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ROYAL COMMISSION ON TRANSPORTATION

OTTAWA, ONTARIO,
TUESDAY,
FEBRUARY 28, 1950.

THE HONOURABLE W.F.A. TURGEON, K.C., LL.D.	-	CHAIRMAN
HAROLD ADAMS INNIS	-	-COMMISSIONER
HENRY FORBES ANGUS	-	COMMISSIONER

G.R. Hunter
Secretary

P.L. Belcourt
Asst.Secretary

COUNSEL APPEARING:

F.M. Covert, K.C. G.C. Desmarais, K.C.	Royal Commission on Transportation
H.E. O'Donnell, K.C. H.C. Friel, K.C.	Canadian National Railways
F.C.S. Evans, K.C. I.D. Sinclair	Canadian Pacific Railway
C.D. Shepard Wilson McLean, K.C.	Province of Manitoba
M.A. MacPherson, K.C.	Province of Saskatchewan
J.J. Frawley, K.C.	Province of Alberta
F.D.Smith, K.C.	Province of Nova Scotia; Transportation Commission of the Maritime Board of Trade
J. Paul Barry	Province of New Brunswick
C.W. Brazier	Province of British Columbia

Ottawa, Ontario,
Tuesday, February 28, 1950

MORNING SESSION

---The Commission resumed at 10.30 a.m.

THE CHAIRMAN: Yes, Mr. Evans?

MR. EVANS: Before I call Mr. Liddy, my lord, I should like to put into the record the rough suggestion for amending the Maritime Freight Rates Act that I promised to give you yesterday. I put it forward subject to this, that as I said when I promised to give it, one would want to look at what scheme was adopted and also the possible effect, what would be required to be done, before one made a final expression of views.

MR. BARRY: Would you please speak a little louder, Mr. Evans?

MR. EVANS: It is pretty difficult to speak so that I can be heard back there.

THE CHAIRMAN: You might do the best you can.

MR. EVANS: If the Commission would look at the Maritime Freight Rates Act and bear in mind that Section 3 provides for the cancellation of existing tariffs and subsection 2 authorizes the Board to have certain powers and (a) of 2 authorizes the Board to approve the cancellation of the existing tariffs, and subject to the provisions of the Railway Act --

THE CHAIRMAN: I am sorry; you are now referring to a section of the Maritime Freight Rates Act?

MR. EVANS: Yes.

THE CHAIRMAN: What section?

MR. EVANS: Section 3. You see the first subsection provides for these preferred movements, and for the cancellation of tolls and for the substitution of new

tariffs, and (2) authorizes the Board of Railway Commissioners as it then was, to approve cancellations, and subject to the provisions of the Railway Act respecting tariffs of tolls for the carriage of freight where not inconsistent with this Act, to approve all tariffs of tolls so substituted.

THE CHAIRMAN: Yes.

MR. EVANS: (b) provides for the maintenance of these tolls subject to increase or decrease as the cost of operation in Canada should change. Then (c) provides for adjustment or variation in these tolls to meet new industrial or traffic conditions. My suggestion for rough consideration is that (c) might provide the vehicle for the amendment, and reading (c) as it stands I would amend it in this way:

> "Adjust or vary such substituted tolls or rates from time to time" --

That is exactly as it is there. Then these are the new words:

> "as may, in the opinion of the Board, be necessary to give effect to any general readjustment of rates in Canada or" --

and this is reading on with the section as it now stands --

> "as new industrial or traffic conditions arise, but always in conformity with the intent of this Act as expressed in sections 7 and 8 and other relative sections thereof."

I offer that amendment, and I would be happy to have discussions with anybody who may see some difficulty in that. I think it is a simple amendment and might be acceptable. I offer it mainly as an indication of the character of the amendment which I think one might have to

[illegible] ... now. [illegible]

[illegible] ... and Transcript [illegible]

[illegible] ... of freight where not [illegible]

[illegible]

THE [illegible] [illegible]

MR. EV[illegible] (c) provides for the maintenance [illegible] these tolls ought to be increased or decreased [illegible] [illegible] should change. Then (e) provides for adjustment or revision in these tolls to meet new industrial or [illegible] conditions. My suggestion [illegible] consideration is that (e) might provide the vehicle for the amendment [illegible] reading (e) [illegible] would amend it in this way:

"[illegible] with substituted tolls or [illegible] time to time [illegible]"

That is exactly as it is there. Then [illegible] the new words:

"as may, in the opinion of the Board, be necessary to give effect to any general readjustment of [illegible]"

[illegible] the section [illegible] now [illegible] industrial or traffic conditions [illegible] in conformity with [illegible] of this [illegible]

[illegible] that [illegible]

[illegible] I think it [illegible]

[illegible]

have in mind to give effect to an equalization proposal.

THE CHAIRMAN: You seem to think that as the Act reads now the Board has not got sufficiently wide powers in case of a general revision of freight rates, and so on?

MR. EVANS: I think there is considerable doubt about that.

THE CHAIRMAN: I think there is.

MR. EVANS: I think my maritime friends would be the first to say that it should not be done, but I think an amendment of that kind, simple in language but general in terms, might be adequate while preserving --

THE CHAIRMAN: Have you any copies of it?

MR. EVANS: I have not -- oh, there are some copies, I am told. I will call Mr. Liddy.

MR. BARRY: This is a matter that I assume could be left for discussion or argument later.

THE CHAIRMAN: Yes.

MR. BARRY: It has occurred to us if there is legislation to arise out of this Commission, as there undoubtedly will be --

THE CHAIRMAN: Please speak louder.

MR. BARRY: If, as there undoubtedly will be, there is legislation arising out of the report of this Commission, it might be that such a matter could be dealt with in that particular legislation without the necessity of a general amendment of the Maritime Freight Rates Act which would continue to operate. However, I do not intend to argue it now. It is a matter that has given us something for discussion later.

MR. EVANS: That is all it is submitted for.

MR. COVERT: It occurred to me that while we are discussing amendments this might be the proper time to

bring up a matter about which Mr. Evans has written to me. He wrote Mr. Frawley under date of February 27 and sent a copy of the letter to me. He refers to a part of the transcript of December 9, Volume 63, at which time your lordship will remember that you suggested to Mr. Frawley, and I will read one paragraph:

> "Now then, you will be giving copies,of course, to the railway counsel and to other provinces and if anybody sees any point in this draft that ought to be discussed now, well we have a discussion but in the meantime you want to proceed."

Then later on you said, Mr. Chairman:

> "As we go along, I intend to continue to ask you if you can really give us any amendments.
>
> "Mr. Frawley; Yes, sir, I have some prepared now."

Mr. Evans has suggested that before the Canadian Pacific case is closed any draft amendments should be submitted so that if it becomes necessary to offer any evidence in connection with them they can do so. I thought perhaps that matter should be mentioned at this point.

MR. EVANS: I had thought, my lord, that we are getting on, and the time might have arrived when our friends would have crystallized their amendments so they could let us see them. I would hope they would not leave these matters until argument because one cannot analyse a section of the Railway Act in relation to amendments without/very considerable amount of additional work, and I think it should be done, if it can be done, as Mr. Covert has pointed out in my letter, before our case is closed. It may conceivably be that

the evidence of a practical witness may be necessary on certain matters to understand a problem created by an amendment. I had not intended to mention this this morning until Mr. Covert mentioned it to me. I think it is an important matter.

THE CHAIRMAN: Is there any reason that occurs to anybody why all proposed amendments should not be in before we adjourn?

MR. SHEPARD: Perhaps I might say something on that matter. My friend Mr. Evans sent me a copy of his letter to Mr. Frawley, and I spoke to him before court convened this morning about it. So far as Manitoba is concerned, I think we can probably certainly put into the record before the adjournment prior to argument any amendments that we will be putting forward in argument, but it may be difficult for us to have them all drafted before the C.P.R. evidence is finished. I explained that as a simple problem of time available to Mr. Evans. We will certainly do our best to get them in, but it may not be possible.. As I understand it Mr. Evans suggests that he would like to have all suggested amendments to the Railway Act and other legislation on the record before the C.P.R. closes its case, and it may not be possible for us to have all that ready.

THE CHAIRMAN: Did you say that?

MR. EVANS: Yes, sir. I think it is important because, as I say, it may become necessary to put a witness in the box to describe the circumstances that may have to be taken into account. I do not know what they might be, but I envisaged the possibility that some evidence might be ncessary to enable the Commission to understand a problem that perhaps has not been considered before.

[illegible]

MR. [illegible]: In th[illegible] [illegible] reason th[illegible] [illegible] proposed [illegible] not be [illegible]

[illegible] it may be difficult for us to have that all [illegible] important problem of the [illegible] may not be possible for us [illegible]

MR. [illegible]: [illegible]

[illegible] necessary to make th[illegible] [illegible]

THE CHAIRMAN: Has anybody else anything to say?

Mr. MACPHERSON: I was going to say that so far as Saskatchewan is concerned we will endeavour to have any amendments available, but this is what strikes me, that during the interval when we are preparing for argument, and when we will be devoting all our attention to a consideration of the evidence, then it may be, and very probably will be, that further amendments will suggest themselves to us. We would not feel like being precluded in any sense from submitting amendments even after the close of the case up until argument because very reasonably in a consideration of the evidence and of the problems represented in the evidence, at the very last minute some amendment may occur to us.

MR. EVANS: It is the last minute amendments that are really dangerous in my view. They have their evidence in largely except on one subject, and it seems to me they must know now what they do recommend.

THE CHAIRMAN: You cannot tell how much difficulty there might be in an amendment until you have seen it, of course.

(Page 16595 follows)

MR. EVANS: That is my problem.

THE CHAIRMAN: That is a matter we will have to speak to when the time comes, but I am glad of this opportunity to say that we think that these amendments cannot be brought in too soon. Mr. Frawley has already given us a number and Mr. Shepard has given us some.

MR. FRAWLEY: I have not seen the letter which Mr. Evans has written to me. I assume it is in my box at the hotel just now. If Mr. Evans was completing his case this week, Friday evening, it might be difficult for me to put into the record before that time the amendments which I have been working on, but I would think that this being Tuesday, a week from today I should be able to put into the record the several amendments which I have prepared.

THE CHAIRMAN: I certainly would be very happy if I understood that all amendments would be in by next Tudsday, that is, all that are in view now subject to what may come out later, which I think will then have to be spoken to.

MR. SMITH: My position, Mr. Chairman, is identical with that of Mr. Shepard's. I, together with Mr. Matheson, have to put in some amendments both for the Province of Nova Scotia, and for the Maritime Transportation Committee, and I think I should at least have until the adjournment for that opportunity of consulting with him and putting in the amendments. I am quite prepared in every way to expedite the matter.

MR. BRAZIER: My lord, I just have one or two very simple amendments that I am going to offer to the Commission, and I am sure I can let Mr. Evans have those

before he closes his case.

THE CHAIRMAN: Well, I think everybody realizes the advisability of having these amendments in as soon as possible. It may be that later on it will be necessary to introduce others, and they will then have to be considered. I think that is as far as we can go, Mr. Evans.

MR. S. J. W. LIDDY CALLED

EXAMINATION BY MR. EVANS:-

Q. Your full name please?

A. Samuel John Wilford Liddy.

Q. And you are the Assistant Comptroller of the Canadian Pacific?

A. Yes, Mr. Evans.

Q. And you were the principal accounting witness for the Canadian Pacific in the 21 Percent Case and in the 20 Percent Case?

A. That is right.

Q. And you have been Assistant Comptroller since when?

A. 1940.

Q. And you are a graduate of McGill University with a degree of Bachelor of Science in Engineering?

A. That is right.

Q. And your service with the Canadian Pacific commenced when?

A. 1914.

Q. And was that full time service or was that part time service?

A. That was part time, Mr. Evans.

Q. In the summer vacations, I gather?

A. In the summer vacations, while attending university.

Q. And then in those vacation periods and following your graduation, I understand you were apprenticed in various departments. What departments were you apprenticed in?

A. I was apprenticed in most departments, Mr. Evans - the Maintenance of Way Department, the Maintenance of Equipment, Transportation Department and also certain outside offices of the Railway.

Q. Then, when did you commence your full time service with the Accounting Department?

A. I commenced my full time service in 1919.

Q. And I gather in 1925 you became a statistician in the Accounting Department?

A. Yes, sir.

Q. And in 1935 General Statistician?

A. Yes, sir.

Q. And in 1938 assistant to the Assistant Comptroller?

A. Yes.

Q. And, in 1940, as you say, you were appointed Assistant Comptroller?

A. Yes.

Q. On page 16188, my lord, of Volume 81, your lordship asked that we provide a study showing passenger losses, and I thought before I go on with Mr. Liddy's evidence, I might file as an exhibit a statement entitled:- "Apportionment of Railway Operating Revenues and Railway Operating Expenses Between Passenger Services and Freight Services, year 1948".

...EXHIBIT 180....filed by Mr. Evans : Apportionment of Railway Operating Revenues and Railway Operating Expenses Between Passenger Services and Freight Services, year 1948.

Q. Now, Mr. Liddy, as the footnote shows on that Exhibit, that apportionment was made on the same basis as was used in connection with the Hearings before the Board in the Rate Cases when similar apportionments were made?

A. Yes, Mr. Evans, similar to the apportionment that was made in Edhibit 138 in the 21 Percent Case.

Q. Now then, I draw attention to the second footnote, which says, that in 1948 only 32% of railway operating expenses are directly separable in the Company's accounts between the two classes of service. The balance of 68% was of a nature incurred for the Company's rail services in general, and could only be apportioned upon an arbitrary and theoretical basis. Mr. Liddy, when you say that 32% of the railway operating expenses are directly separable, what do you mean?

A. Well, take an account like Passenger Train Car Repairs. That is directly separable to Passenger Services.

Q. And do you say then, that of the total expenses related in this exhibit, 32% are in that category which are directly allocable and the others are apportioned on a theoretical basis?

A. That is right.

Q. Now, looking at that Exhibit, Mr. Liddy - -

COMMISSIONER INNIS: Was the 32% arrived at after you made the complete computation?

MR. EVANS: No, 32% are allocable directly from the books.

COMMISSIONER INNIS: 32% of what?

MR. EVANS: Of the expenses.

COMMISSIONER INNIS: Of all expenses?

MR. EVANS: Of the expenses allocated to passenger and the balance, as the Exhibit shows, were apportioned on this statistical basis.

COMMISSIONER INNIS: What I was concerned about was, did you first allocate the amount and get the total and then get the 32% from that?

MR. EVANS: Mr. Liddy, what is your answer to that?

THE WITNESS: No, 32% represents on this Exhibit the proportion of $39,175,356 - -

Q. That is the figure opposite "Expenses Solely Related"?

A. Yes, and the similar figure opposite "Freight Expenses Solely Related" is $65,929,504. That is a total of $105, million. That is 32% of the total operating expenses of $326 million.

COMMISSIONER INNIS: What is the $326 million?

A. That is the total railway operating expenses, freight and passenger.

THE CHAIRMAN: Does that result from a dilation of any figures here? I don't see that figure.

A. That is a computation, Mr. Chairman.

Q. $326 million ?

A. $326 million is the total railway operating expenses and is found by adding the two figures on the Exhibit.

Q. That is what I wanted to know.

A. The first figure to take, is the expenses of passenger service amounting to $91 million odd, and the expenses for freight services amounting to $234 million odd.

MR. EVANS: What you are saying is, that 32% of those total expenses is directly allocable as between passenger and freight on the books?

COMMISSIONER INNIS: So it is 32% of the $326 million?

MR. EVANS: Yes, is directly allocable to one or the other. Now, I gathered, although the figure does not show, Mr. Liddy, that one arrives at the passenger deficit by subtracting the revenue figure of $23,617,211 from the expense figure for passenger of $91,484,172?

A. Yes, that is right, or perhaps the other way round - subtracting the $91 million from the $62 million.

Q. And you get a minus figure?

A. That is right.

Q. And that leaves, as I have it, and you will check me if I am wrong, the passenger deficit in the year 1948 on the basis shown by this Exhibit, would be $28,866,961?

A. Yes, sir.

Q. Now then, that is the deficit for the whole of Canada, is it not?

A. Yes, sir, for the Canadian Pacific.

Q. For the whole of Canada for the Canadian Pacific. Now then, the figure shown at page 185 of Part I of the Canadian Pacific Brief for Western Canada - you will see it in the middle of the page - is $18,555, 654?

A. Yes.

Q. And I gather that if one wants to derive the deficit in Eastern Canada, one could do so by taking the $18 555,654 from the figure of $28,866,961?

A. Yes, Mr. Evans.

Q. And I make it that the Eastern deficit in 1948 was $10,311,307?

A. That is right.

MR. BRAZIER: Mr. Chairman, could I ask at this point, could Mr. Liddy produce a statement similar to that on page 116 of the Appendix to Part I to get a similar comparison?

MR. EVANS: He could, Mr. Brazier, but the amount of work necessary to do that would be out of proportion to the value of it, because we have the deficit for the whole of Canada. All we have to do is subtract one figure from the other.

MR. BRAZIER: It does not appear to me that all the incidental expenses are included or the incidental revenues included here as they are in 116. There does not appear to be mail or express revenue in that one on page 116.

THE CHAIRMAN: You are referring to page 116 in what?

MR. BRAZIER: In the Appendix to Part I of the Canadian Pacific Submission. It appears to me that it is not an exact comparison, and that we are not getting really a true figure by merely subtracting as Mr. Evans has done.

MR. EVANS: Now, I am sure Mr. Brazier can ask Mr. Liddy that in cross-examination, but, Mr. Liddy, are results which were obtained on page 116 of the Appendix to Part I on a comparable basis with those shown on Exhibit 180?

A. Well, it is true, as Mr. Brazier says, that there are small amounts of incidental revenue. I think they amount to about $7 thousand, but not enough to affect the basis, Mr. Brazier.

MR. BRAZIER: Mail and express are in these figures in the Appendix?

A. That is right.

MR. EVANS: What you were trying to do, Mr. Liddy, if I understood you, is you were trying to give to this Commission, the same kind of exhibit that was given to the Board in the Rate Cases?

A. Yes, sir, strictly comparable to Exhibit 138 in the 21 Percent Case.

Q. Now, before I leave that Exhibit, Mr. Liddy, I would like to ask you whether you have anything to say as to whether the results which this exhibit shows are on an out-of-pocket basis?

A. No, this Exhibit is prepared on the basis of a total income.

Q. It is Exhibit 180 you are speaking of now?

A. Yes, Exhibit 180 is prepared on the basis of total income. I would like to draw perhaps, the Commission's attention to the first figure in expenses which are designated "Solely Related", that is, the figure $39,175,000. That is part of the total out-of-pocket costs.

Q. When you speak of "out-of-pocket", you mean in the general sense, that the expenses would be saved if you could stop giving passenger service?

A. Yes, and the expenses that would be added if you added passenger service or the expenses that could be curtailed if you cut down passenger service.

Now, the out-of-pocket expenses would lie somewhere between $39 million and the total apportioned expenses of $91 million - somewhere between those two figures. None, as far as I know, has ever adopted the rule or found the formula in which they are satisfied that they could determine what out-of-pocket expenses are, but, in my view, out-of-pocket expenses would lie closer to the $39 million that they do to the $91 million.

Q. Then, Mr. Liddy, we can pass on to page 60 of Part I of the Company's Brief. Now then, before I ask you any questions, I take it that in your position, as Assistant Comptroller, that you are the accounting officer who is responsible for the accounting material and for the submissions contained in the Brief of the Canadian Pacific?

A. Yes, I am. The statements on accounting subjects in the Brief represent my views and the figures and data in the Brief in support of those statements were either prepared by myself or under my direction.

Q. Now then, in the middle of page 60 there is a paragraph which begins in the second sentence as follows:-

> "It may seem to the superficial observer simple to ascertain what is the actual cost of service. In fact, however, the problem of disentangling joint costs is one of great magnitude and complexity, and unless the volume of traffic being considered is a fairly large proportion of the total traffic moving over the railway, an allocation of many costs must be made on the most arbitrary basis. It has been stated on numerous occasions by accountants and economists that railway operations do not lend themsleves to cost accounting"

Now, can you assist the Commission in explaining what is meant by that statement in our Brief?

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(Page 16605 follows)

A. Yes, I think I could perhaps help the Commission in understanding this problem of disentangling joint costs by pointing out how we keep our accounts and why we so keep them.

Q. What is the first thing you would like to draw attention to?

A. First I would like to touch on the details we have of the cost of railway property.

THE CHAIRMAN: Q. The cost of what?

A. Railway property. For the year 1948, as of January 1, 1948, the total cost of railway property of the Canadian Pacific Railway amounted to $1,271,991,255.

MR MACPHERSON: Q. Is that historical?

A. Yes. This investment is classified in our books under some forty-five headings. I have a statement showing this investment which I would like to file as an exhibit.

MR EVANS: That will be Exhibit 181. It is entitled "Details of Investment in Railway Property as of January 1, 1948."

---<u>EXHIBIT 181</u>: Details of Investment in Railway Property as of Jan. 1, 1948.

MR EVANS: Q. Now, Mr. Liddy, what have you to say about this exhibit?

A. The headings shown on this exhibit are in accordance with the primary accounts contained in the classification prescribed by the Interstate Commerce Commission for railroads in the United States. I believe it would be helpful at this time if we filed copies of the Interstate Commerce Commission accounting classification for steam railways.

Q. Have you some copies there?

A. Yes.

MR EVANS: I am sorry to say that we had not

enough copies to supply to my friends. We supplied them with copies of the other exhibits, but we had not enough copies of these rather voluminous exhibits.

THE WITNESS: I might say, Mr. Evans, that copies of this classification can be purchased from the Association of American Railways for a nominal price.

MR EVANS: That will be Exhibit 182.

---EXHIBIT 182: Interstate Commerce Commission accounting classification for steam railways.

MR FRAWLEY: Q. Is there any place else you could purchase them, Mr. Liddy?

A. Well, I see that information, Mr. Frawley, on the inside cover of the folder here.

MR MACPHERSON: Mr. Chairman, there is a question that I think might very well be raised now in connection with this Exhibit 181. It presumes to set out what Mr. Liddy gives as the historical investment cost of the railways. Now, what I would like to know, and what my colleagues would like to know, is to what purpose this evidence is being directed in so far as the Commission is concerned. I note that on page 64 of Part I the company says:

> "It is submitted that no amendment is necessary to the Railway Act of Canada to apply the principle of fixing general rate levels . . ."

That is to say, if the evidence is being directed for the purpose of establishing the rate of return or rate base or anything of that kind, then it will open up a great field for cross-examination that probably otherwise might not be necessary; and it is difficult for us to understand why this should be gone into, in the light of the fact that at page 64 it is claimed in the outline by the company itself that no amendment is necessary to the Railway Act of Canada to apply the principle. Now, is it being

directed to the question of the establishment of rate base and the rate of return, and what is the purpose of it?

MR EVANS: My friend is most impatient. I have only just introduced the exhibit, and I think if my friend possesses his soul in patience he will find that I am not going to spend very much time on it, but there is a good deal in the brief about how the rate base is made up, and I can tell him now that within the next minute or so he is going to find that we are still dealing with---

THE CHAIRMAN: Pardon me. Can you hear?

MR MACPHERSON: Not very well.

MR EVANS: We are still dealing with this question of disentangling joint costs, and I just suggest that my friend possess his soul in patience for about one minute and he will find that we will not spend much time on it.

MR MACPHERSON: I wish to point out that it is not a question of being impatient; it is a question of ascertaining why my friend is endeavouring to establish the investment in railway property as $1,271,991,255. If he does not know now -- and I think he does, from our experience before the Board of Transport -- we do not accept that figure, and if he is endeavouring to establish that figure as representing details of investment in railway property, which would be considered as a rate base for rate of return, then I only wish to point out now that that will be challenged now, as it has been before.

MR EVANS: I never expected my friend would not challenge almost anything I said; he has always done it, and I guess he always will; but---

MR MACPHERSON: Oh, well---

MR EVANS: Now, just a minute. I am going to have a word here, if you please.

MR MACPHERSON: My only point is that I resent

the suggestion---

THE CHAIRMAN: If you gentlemen will only speak one at a time it will make it easier for all of us. Go on, Mr. Evans. What were you going to say?

MR EVANS: I was going to say, my friends are extremely sensitive when any figure of rate base is mentioned; they were before the Board of Transport Commissioners. They shudder at the very thought of it.

Q. Now, Mr. Liddy---

THE CHAIRMAN: You refer, Mr. MacPherson, to page 64, where there is a paragraph set out numbered 45; that is what you have in mind, is it, where it is said:

> "It is submitted that no amendment is necessary to the Railway Act of Canada to apply the principle of fixing general rate levels on the basis of a fair return on the investment in railway property used in transportation service."

That is, Mr. Evans assumes that that is the principle that has always been followed or ought to be followed in cases that arise, and then he says that the determination of the investment is a matter for the Board. I do not think this exhibit interferes with that statement at all.

MR MACPHERSON: Well, my lord, all that I wish to know is the purpose that is being served by establishing this investment now, the purpose that it is intended to serve before this Commission.

THE CHAIRMAN: Bear in mind that this Commission is not fixing anybody's rates, you see; we are just dealing with matters of the principle that ought to be followed when rates are fixed; that is the idea. Therefore information of this kind might be said to be of secondary interest, but it is of interest to us, because we are probing the railway situation in Canada as fully as we can, for very many

purposes.

MR MACPHERSON: Well, my lord, as long as---

THE CHAIRMAN: Whether this statement shows more or less money invested historically does not affect any principle. I do not see that it can do you any harm. What danger do you see in letting this exhibit in?

MR MACPHERSON: Well, my lord, the point that I wish to raise is that the information which is almost identical with this was used by our friends before the Board of Transport for the purpose of endeavouring to establish a rate base on which a rate of return could be given. Now, my purpose in raising the query now was to ascertain what purpose was being served by this evidence now: Was it being submitted on a basis of consideration being asked for this amount being taken as the rate base on which return should be given? And if that is the purpose, I wish to say that it will be challenged, as I said before.

THE CHAIRMAN: We are not fixing rates or figures on which rates ought to be based; we are just, I repeat, dealing with principles. Now, the C.P.R. submits in its brief that there is a certain principle which I understand has always been followed and applied, and it goes on and says that the amount in each case is something for the Board to determine. Are you departing from that in any way?

MR EVANS: No, sir. I can say to my friend and say to the Commission that we have dealt with this question of fair return and rate base; we have dealt with the question of disentangling joint costs. We thought that unless we could show the information which goes to make up these things the Commission would not understand what our submissions were about, and it is for the information of the Commission. We do not ask the Commission to find what our

rate of return should be or anything else.

MR MACPHERSON: My lord, there is just one point I would make in connection with it. The almost identical figures with these were presented to the Board of Transport in the 20% Case, and the Board was asked to accept these figures as a rate base and to establish a rate of return. The Board did not do so, and expressly refused to accept the figures or to grant a rate of return based on this rate base.

THE CHAIRMAN: What did it do, then?

MR MACPHERSON: On the basis of requirements; they proceeded on the basis of requirements and not on the basis of a rate base, and they never have.

THE CHAIRMAN: Well, we do not see any reason at all for you to think that any prejudice is being caused, Mr. MacPherson, by the filing of these figures. They are informative for us. But when you bear in mind that anything that comes out of our study will have to lead to principles and not to establishing any figures in favour of anybody or against anybody, I think you will understand that this cannot do you any harm, while it will give us certain information.

MR MACPHERSON: I might refer, my lord, just at this point to the judgment of the Board in the 20% Case, at page 15.

THE CHAIRMAN: Yes; what do they say?

MR MACPHERSON: They say:

> "However I do not believe that such considerations justify me in determining without further evidence and investigation that the investments have been prudently made, and that the revenues have been sufficiently accounted for."

MR EVANS: Now, if my friend wants to argue ques-

tions of prudent investment I will be very glad to do it, but I did not think this was the time or the place. I do not know why my friend persists in suggesting that the Board has rejected our views on this subject, because there is a great deal that I could point to that I do not think would do more than just waste the time of this Commission. I am quite prepared to do it, and I am quite prepared to argue the question with my friend, but I did think---

THE CHAIRMAN: I think, then, that the difference between you probably is this, that on the one hand we have the suggestion that the proper basis is a fair return on the investment in railway property used in transportation service, and Mr. MacPherson thinks the principle ought to be simply the requirements from time to time. Is that right?

MR MACPHERSON: Well, as a matter of fact, what I say is that the Board of Transport has determined the issue on the question of requirements.

THE CHAIRMAN: Then you seem to approve of that determination.

MR MACPHERSON: Well, it was on that basis we do not accept the rate base as it is represented in the figures given here.

THE CHAIRMAN: Well, there is nothing in the filing of this exhibit to preclude you from arguing on that question any way you like.

MR MACPHERSON: Well, of course, what I want to make clear, my lord, is this, that since my friend has filed this showing the investment at $1,271 million, it will be necessary for us to deal probably at some length with this exhibit in cross-examination.

THE CHAIRMAN: Well, that is all right; but I do

not see how it affects the principle very much whether you add a few million to that statement or subtract it; the principle remains the same. We will let the exhibit in, and then you will have full liberty of cross-examining, of course.

All right, Mr. Evans.

MR EVANS: Q. Now, referring to Exhibit 182, the classification of accounts that you have just filed, where in that classification of accounts will you find the text pertaining to the accounts for investment in road and equipment?

A. The accounts for investment in road and equipment in this classification will be found commencing at page 19 of Exhibit 182 and extending over to page 48.

Q. Now, does the prescribed classification which we have been talking about provide for the segregation of investment by primary accounts between passenger and freight?

A. No, Mr. Evans. It is designed to show the total investment irrespective of whether or not facilities are used for passenger or freight services. For example, on page 21 of Exhibit 182 the account grading, that is account No.3 in the classification, covers the entire cost of constructing the roadway below the ties and ballast; it includes expenditures out on the line as well as expenditures in the yard. The major portion of the investment in grading is, of course, naturally common to both passenger and freight service, although in some instances you may have a passenger station or a particular freight station.

Q. Before I go on with that subject: How does the Interstate Commerce Commission method of segregating passenger and freight expenses operate? Perhaps you could give some practical description of how it differs from the

way your accounts are put?

COMMISSIONER INNIS: This is with reference to grading?

MR EVANS: No, no. I said before we went on to another subject I just wanted to ask him how the segregation of passenger and freight expenses under the Interstate Commerce Commission regulations differs from the way the company has its segregation in its books.

THE WITNESS: Well, this Exhibit 182, being the uniform system of accounts for steam railways as prescribed by the Interstate Commerce Commission, does not deal with this subject of segregation between freight and passenger.

MR EVANS: Q. How is that done? By regulation of some kind?

A. That is done by a rule, yes, a rule of the Interstate Commerce Commission.

Q. And what does it involve as far as accounting is concerned? Could you give an example of how, for instance, a yard would be treated in their accounts as compared with the way you treat it in yours?

A. They would ask the carriers to keep separate accounts, separate books, for the maintenance of their yards, separate from the maintenance of their road, and you might find in a large terminal that they would have three or four different kinds of yards, a passenger yard and a freight yard, perhaps a common yard.

(Page 16616 follows)

Each one of these cases would have separate books. The Interstate Commerce Commission ask that the expenses that are solely related to passenger in respect say of the maintenance of yards would be put in a column solely related to passenger.

Q. So that it starts right in at the bottom, as it were, and moves up through the accounts as a regular matter in regard to a large proportion of the common expenses?

A. That is right.

Q. Without going into detail, roughly what proportion of accounts or of expenses are directly allocable under the I.C.C. system? If you do not know it does not matter, but would it be substantially more than the 32 per cent you showed on an earlier exhibit?

A. Yes, by that method they would get substantially more.

Q. And leaving the rest for statistical division?

A. That is right.

Q. To go back to these investment accounts that we were talking about, you have told me about grading, and how grading is common to both passenger and freight. What about the other investment accounts, Mr. Liddy?

COMMISSIONER INNIS: Would grading be divided equally?

MR. EVANS: I do not know how it would be divided. I would not think it would be divided equally.

Q. How would you, for instance, go about dividing grading costs if you wanted to segregate them as between passenger and freight?

A. You mean, Dr. Innis, under Canadian Pacific practice?

COMMISSIONER INNIS: Q. Yes.

A. We would divide grading in accordance with the

gross ton miles in freight service as compared with the gross ton miles in passenger service.

Q. Roughly it would be simply that proportion?

A. That is right. Throughout time there have been many, many opinions as to how an expense like that should be divided. I think one of the earliest conceptions was that perhaps train miles was a good yardstick to divide this expense. Then they got the idea that perhaps the consumption of coal would be a good measuring device, consumption of coal representing the energy spent in hauling trains. Well, they did not like that so now they are down to gross ton miles, and where they will go to-morrow I cannot say.

Q. The question of speed would not mean that the passenger might be entitled to more? Do you need heavier grading for the speed involved in passenger trains?

A. I think that was the idea in the minds of those who were advocates of the fuel consumption as the index.

MR. BRAZIER: Mr. Evans, is Mr. Liddy now speaking of investments or operating expenses?

MR. EVANS: As you will find in the record, I went back to the question of investment accounts, and this interjection was a question of Dr. Innis as to how they would divide the expenses for grading.

MR. BRAZIER: There is no doubt he is not speaking of the investment account, the segregation of that.

MR. EVANS: His answer to me had to do with the investment account. His answer to Dr. Innis was on another subject.

Q. Having discussed the investment account for grading you were about to tell us about the other investment accounts in this connection, the division between passenger and freight?

A. Yes; there are a few exceptions in the other investment accounts.

Q. Such as?

A. Such as grain elevators. Grain elevators would be all freight. Likewise freight train cars would be all freight. Passenger train cars would be all passenger. In general, however, if one looks down the list of these primary accounts in investment and railway property one will be struck by the fact that the vast majority of these accounts are common and they do not distinguish between freight and passenger service costs.

Q. Now then, having discussed the investment account does the situation that you have described also pertain to operating expenses?

A. Yes, it does. I should like to refer the Commission to the operating accounts which commence ---

Q. You are now referring to Exhibit 182?

A. Yes, Exhibit 182, at page 91, and they run over as far as page 163.

Q. The expenses for the year 1948 for the company were what?

A. For the year 1948 railway operating expenses of the Canadian Pacific amounted to $326,000,000. The details of these expenses by primary accounts are shown in the annual report which we make to the Dominion Bureau of Statistics and to the Board of Transport Commissioners.

Q. Have you got a copy or so there that you would like to file?

A. Yes, I have a few copies.

MR. EVANS: That will be Exhibit 183.

EXHIBIT NO. 183 -- Report of C.P.R. to Dominion Bureau of Statistics and Board of Transport Commissioners.

THE CHAIRMAN: Q. How do you describe it?

A. This report is captioned, "Canadian Pacific Railway Company annual report to the Dominion Bureau of Statistics and to the Board of Transport Commissioners for Canada, 1948."

MR. EVANS: Q. That is the year 1948 you have?

A. Yes.

Q. What does that exhibit show, Mr. Liddy?

A. The Commission will find the operating expenses set out in Schedule 17 of this report. The pages in this report are not numbered. You will have to look for the schedule.

THE CHAIRMAN: Q. What number did you say?

A. Schedule 17. In Schedule 17 we have first maintenance expenses. The primary accounts in maintenance of way and structures are designed to show expenses of maintaining road property devoted to railway operations whether such operations pertain to freight or passenger service or both.

Q. That is 17A, is it?

A. 17A deals with maintenance of way. 17B deals with maintenance of equipment, and C and D and so on.

Q. When you refer to schedule 17 you mean 17A?

A. A, B, C and D.

Q. For the present what are you reading?

A. I am dealing first with 17A.

MR. EVANS: Q. Having said something about the primary accounts not being separable between railway and passenger as such what are they useful for?

A. They are useful for management control purposes in respect of labour and material items. It will be noted, for example, that the maintenance of structures such as tunnels, subways, bridges, trestles and

culverts are shown separately from maintenance of track property which includes the cost of renewing ties, rails, other track material and ballast, and the labour cost of laying such track elements.

Q. There are separate accounts provided?

A. Yes. Separate accounts are provided for these items, and separate accounts also are provided for the maintenance of buildings, stations, shops and engine houses, and many other items of that kind. It will be readily appreciated that the main objective of such a classification is not to show the cost pertaining to any particular service such as passenger and freight service, but to provide management with the basic information required for efficient operation of the railway property.

Q. Now then, with regard to maintenance of equipment -- you have been talking about maintenance of way -- what do the expenses for maintenance of equipment consist of?

A. Maintenance of equipment expenses largely fall into five items. The first item is shop machinery and power plant machinery; second, steam locomotive repairs; third, freight train car repairs; fourth, passenger train car repairs and fifth, work equipment repairs. Apart from the maintenance of freight and passenger cars the remainder of maintenance of equipment is common to all transportation services.

Q. Having dealt with maintenance of way expenses and maintenance of equipment expenses, what about traffic, transportation and general expenses?

A. A glance down the primary items of traffic, transportation and general expenses reveals a similar situation exists as for the maintenance accounts. Thus the classification as a whole provides for the recording

of operating expenses according to the nature of expenditures irrespective of whether such expenses result from the transportation of agricultural products, mine products, domestic or export traffic, carload or l.c.l., transportation of property or persons.

Q. Is it fair to say that the accounting classification was designed for management control purposes, as you have called it, rather than for cost accounting purposes?

A. Yes, quite. While the classification segregates railway expenses and investments into a large number of accounts most of these are necessarily joint or common to all operations.

Q. Now, before we go on, you have been speaking about management control. Perhaps that is a term of art in the accounting profession. Would you indicate what you mean by management control?

A. Well, take, for example, the cost of coal. We purchase the same kind of coal for freight or passenger engines, and it is essential for management to have statistics which will indicate whether or not the operating man is getting the most number of ton miles out of the coal that is consumed in his district, and that the mechanical man will design the most efficient engine --

THE CHAIRMAN: Q. Will design what?

A. The most efficient engine.

MR. EVANS: Q. So what you mean by management control is to enable management, as it were, to police expenses?

A. That is essentially the function of the classification.

Q. Now, having discussed the difficulties of

disentangling joint costs and having pointed out that the classification does not provide any basis for cost accounting purposes, what do you as a practical railway accounting officer say about this cost of service principle that has been advocated?

COMMISSIONER INNIS: You have already submitted some evidence as to the efficiency of your cost system, have you not?

MR. EVANS: The efficiency of the cost system?

COMMISSIONER INNIS: That is to say, some indication as to how closely you can adjust your expenses to the traffic?

MR. EVANS: You are thinking of the extent to which costs are variable with traffic?

COMMISSIONER INNIS: Yes. That is to say, is there any way of indicating how efficient your cost system is as an instrument of management control?

MR. EVANS: Perhaps I should get you to put that question to the witness, but I am not quite clear as to what you have in your mind. What the witness has been saying is that the prime purpose of the accounting classification is to provide primarily a method by which management can control expenses rather than to get into a cost accounting division as between the different services.

COMMISSIONER INNIS: That is precisely what I was wondering about. That is to say, over the years has your cost system improved as an instrument of control or management, or is there any way of indicating whether it has become more effective?

THE WITNESS: Certainly the efficiency of the railway has continually improved, Dr. Innis, but I take it your question refers particularly to the method of control?

COMMISSIONER INNIS: Q. I am thinking simply of the over-all efficiency of your cost system. That is to say, I presume you build this up in relation to management control, your expenses and so on, and I am only wondering whether you were able to check yourself or to appraise the efficiency with which you have improved it, and the extent to which you have improved it?

A. There are many indices of efficiency, and the Canadian Pacific has open to it the efficiency of American railways, that is, does the Canadian Pacific maintain its freight cars at a cost comparable or less than other railways? Does the Canadian Pacific get as many ton miles per pound of coal as other railways are getting? Is the Canadian Pacific able to operate over all as efficiently as other railways, that is, is its proportion of maintenance of way out of line with the proportion of maintenance of way of other railways? Is its transportation ratio a reasonable ratio? There are many details of that kind, and many officers of the company belong to associations of railways in the United States, and these associations get together and discuss these technical subjects in very minute detail. For example, the dining car superintendents get together and they talk about the cost of providing a meal and how to cut down that cost, and what methods and means they have adopted.

Q. My point is as a result of this investigation and study and so on are you able to show that your variations in expenses are much closer towards variations in traffic? Do you see what I mean? That is to say, what is the general impression of all this machinery you are describing, or the effect of it?

A. You put me in a rather embarrassing position,

Dr. Innis, because the Canadian Pacific believes it is fairly efficient. Others say we are efficient, and we seem to have been used as a yardstick, and our officers tell me when they go to the United States and talk to other officers that we have no apology to make for our methods.

Q. I presume that is perhaps an understatement, but are you free to say whether your technique has improved over the past twenty-five years, or do you find that in certain periods, for example, where traffic is relatively stable, that it is much easier to control? Does it tend to get out of hand at definite periods, and what are those periods? I don't know whether I make myself clear.

A. Well, may I say this, Dr. Innis, that we release to our operating officers a great deal of information and data along statistical lines that never gets up to the stage of an annual report. We are probably the foremost in that field of detailed statistical because we believe that the place to make the money and to make economies is right at point A where the work is being done. We issue reams after reams of statistical data which goes to these various operating officers. We have some 32 officers on the line that operate territories, and we give them very minute data comparing this month's operation with last month's operation wherein they can see whether or not they have done as well or worse, whether their train loading has improved or slipped off. I can assure you that these detailed statistics are looked at very carefully, and always at the back of an operating man's mind is the fact that his record will show in a blue print to be looked at by superior officers.

Q. I understand that, but I was more concerned about your views on the general trend of efficiency of

cost accounting.

MR. EVANS: Perhaps what you wanted to know was whether the system they now have is improved over what has been the case. Do you see what Dr. Innis means?

COMMISSIONER INNIS: That is right.

MR. EVANS: Q. Has your system improved or is it staying static?

A. I would not want to say it is static. I think to-day we are getting statisticians who are perhaps better trained in a technical way than what we could obtain twenty or thirty years ago. These better trained statisticians are bringing out continually improved methods and improved ways to bring out this information to the operating man.

MR. EVANS: Does that answer your question?

COMMISSIONER INNIS: Yes.

COMMISSIONER ANGUS: Q. You think it still remains safe to say, as has been stated on numerous occasions, that railway operations do not lend themselves to cost accounting?

A. Yes. One has only to sit down quietly in an armchair and think that over, Dr. Angus, and he must inevitably come to the conclusion that there is no way of separating grading, there is no way of separating wear and tear on a rail.

COMMISSIONER INNIS: My concern was rather with the over-all picture as to whether you were improving your whole technique and making it possible to get a much closer adjustment between expenses and traffic over a considerable period.

MR. EVANS: Your question, Dr. Angus, had reference to cost accounting --

COMMISSIONER ANGUS: Whether improvement in

methods of investigating and so on had gone so far as to overcome this --

MR. EVANS: Oh, I see what you mean.

Q. Mr. Liddy, what Dr. Angus intended to ask you was whether this statistical activity that you have been speaking of has gone far enough to remove the difficulties with cost accounting?

A. No, sir.

Q. Now, then, I was about to ask you, having regard to what you have said about the difficulty of disentangling joint costs, and how the classification was designed for management control purposes, what is your conclusion as a practical accounting officer as to the possibility of applying the cost of service principle to railway rate making?

A. The cost of service principle from a practical accounting standpoint is impossible to apply. The problem of disentangling joint costs is one of great magnitude and complexity. Any attempt at cost accounting would be a most cumbersome and expensive procedure and would inevitably involve the allocation of so many items on a purely arbitrary basis as to be of little if any value.

Q. Now then, we turn to another subject, Mr. Liddy.

THE CHAIRMAN: Before you do that we will have a few minutes' recess.

---Recess.

(Page 16628 follows)

...UPON RESUMING

MR. EVANS: When we adjourned, I was about to read, my lord, from page 66 of the Company's Brief, Part I, the first complete paragraph on the page. It reads as follows:-

"The book records of the investment of Canadian Pacific in railway property used in transportation service are set forth in Exhibit (49) - 49 filed in the 20 Percent Case. They show that after deduction of depreciation, the investment in the railway enterprise as of December 31, 1947, was $1,001,337,371. It is upon such a depreciated investment base as a minimum that, in the submission of Canadian Pacific, a rate of return should be calculated. The rate of return would, of course, have to be adjusted from time to time to reflect changing economic conditions."

Now then, Mr. Liddy, have you any comments to make for the information of the Commission in regard to the depreciated investment base, so-called?

A. Yes, the figure of $1,001, 000,000, representing the depreciated investment base at December 31, 1947, is made up of the gross investment - -

Q. That is on railway property, you mean?

A. Gross revenue on the railway property which appears on Exhibit 181 and railway working capital less the book depreciation reserves.

COMMISSIONER ANGUS: May I ask one question about Exhibit 181 which I am not clear about? If one railway buys another railway or acquires it, are the assets

taken in at the value they stand in the books of the railway that is acquired or bought, or are they calculated on the basis of the price that is paid?

A. Well, Dr. Angus, the Canadian Pacific has been fortunate that it has never had to sell out, but I believe for United States railways that if they incorporate another railway and buy it, that it is the cost of the investment of the first one to devote that property to transportation service that goes into the books, and then they adjust their balance sheet between that cost and the purchase price.

Q. And these figures in 181, do they include assets of railways which the Canadian Pacific has bought?

A. Yes, this is the property. It includes the property, that is, the investment in bridges and ties of any railways that we have acquired.

Q. And are those included at what they stood in the books of the railways which you acquired or were those figures adjusted to conform to the price you paid?

A. You are thinking now, I take it, Dr. Angus, of some of our leased lines?

Q. Yes, or even lines acquired outright?

A. Well, if we acquired a line outright, and we had the accounts for it, these figures would be the accounts, but take our leased lines in which we are leasing a property. We have an investment in that leased line of so much for stock and so much for bonds, perhaps, and there may be outstanding in the hands of the public other stock and other bonds and what we have done in those cases where we have not had the primary accounts, we have taken the

book value of the stocks and bonds into these figures.

MR. McLEAN: Would that be true of the Ontario and Quebec Railway?

A. We have the accounts of the Ontario and Quebec Railway.

THE CHAIRMAN: That disposes of your leaseholds, but it does not seem to cover the cases where you purchased outright. Have you ever purchased outright?

MR. FRAWLEY: The Coleman North Western was one that you did acquire outright.

A. Well, I take it that the Coleman North Western would keep accounts.

THE CHAIRMAN: What do you suggest?

A. I would presume they would have kept accounts.

MR. McLEAN: Well did they?

A. Well, the question you asked me is did they. I really don't know.

MR. EVANS: If they kept accounts, what would be the way you would reflect the asset value?

A. We would analyze those accounts and classify them in accordance with the accounts on Exhibit 181. We now have that property, we now operate that property, and we would put the expenditures into ties, rails, or wherever the expenditures should go.

Q. So that when you ended, you would have in your accounts the cost of that company, of the railway assets that had been leased to you or the company?

A. That is right.

COMMISSIONER ANGUS: To make it clearer to me, could this happen? If you acquired a railway and made a

advantageous or good purchase, is it possible that the figures that would go into this sheet of investment figures could exceed the price that you paid for the railway?

A. It might be possible, Dr. Angus, but most of our leased lines, so-called, were really built by the Canadian Pacific under separate charters, and the charters were obtained in order that the line might be built. It might not have been possible under the Canadian Pacific charter for the Canadian Pacific to have built in a certain area, but another railway we had hired might have a charter that permitted it to build in that area, and that is the way the Canadian Pacific was built up.

Q. I am not criticizing the practice; I am merely trying to find out what the figures represent?

A. Have I made them clear, Doctor?

Q. Yes, I think so.

MR. EVANS: Now, you have been referring to this figure of $1,001,000,000. Would you tell the Commission, Mr. Liddy, how that figure is arrived at?

A. The figure of 1,001,000,000, includes an allowance of $35 million for stock and materials and supplies required to carry on the company's railway business together with an amount of $35 million in cash required for the same purpose.

Q. That is the working capital. Now then, you add that working capital figure, do you, to the investment shown in Exhibit 181 of $1,271,000,000 odd?

A. Yes, and then get a figure of $3,141,000,000 odd.

Q. And from that you deduct something?

A. Yes, we deduct from the latter figure that I have mentioned the amount of depreciation that now rests or did

rest at December 31, 1947, in our depreciation reserve account, namely $340 million.

Q. That is a round figure you are giving us?

A. Yes.

Q. Now then, how is the gross investment recorded in the books of the Company?

A. As I have already explained, it is recorded in detail by primary accounts divided between road, equipment and general expenses as shown on Exhibit 181.

Q. Now, is all that property depreciable?

A. No, some of this investment is depreciable and some of it is non-depreciable. In this connection, Mr. Evans, we have followed the segregation between depreciable and non-depreciable property as in effect for railways in the United States.

Q. Well, what are non-depreciable?

A. Non-depreciable items are such things as land, ties, rails, other track material.

Q. Then, what about bridges and stations and so on?

A. Bridges, stations, shops, engine house, signals and interlockers are classed as depreciable property.

Q. And equipment?

A. All equipment is depreciable property.

Q. Now, would you give the Commission a segregation in the account as between the depreciable and non-depreciable property? Take the figure to start with of that

$1,271,991,000?

A. Yes, of that figure of $1,271,991,000. the depreciable road amounted to $322 million.

Q. That is a round figure?

A. Yes, and depreciable equipment amounted to $388 million and non-depreciable road amounted to $561 million.

THE CHAIRMAN: That last figure again, please, non-depreciable roads - how much?

A. $561 million.

MR. EVANS: Percentagewise, how does the depreciable compare with the non-depreciable property?

A. The proportion of our gross investment in railway property which is depreciable amounted to 55.9% and the balance or 44.1% was non-depreciable. The 55.9%, Mr. Chairman, is made up of those first two figures I gave you of $322 million and $388 million, making $710 million out of a total investment of $1,271,000,000 or 55.9%.

COMMISSIONER INNIS: How do you handle an item in which the value has increased or which is appreciable?

A. That remains in the books at its original historical cost.

Q. There is no provision made for any such development which might happen in the cost of land.

A. No, sir, the firm basis is cost.

MR. EVANS: Now then, Mr. Liddy, you have spoken of the figure of $340,653,884 as at December 31, 1947, as the amount of book depreciation. Now, what percentage does this figure represent of the total railway depreciable property?

A. It represents 47.9% of the total depreciable property; in other words, the depreciation reserve represents almost one half of the investment in depreciable property.

Q. Now then, having dealt with depreciable property

I would like to turn for a moment to non-depreciable property, and in regard to that, which I understand amounts to $561 million, what provision is made for the replacement of this property as it wears out?

A. Well, a large part of that investment, Mr. Evans, represents rails, ties, ballast, grading and the like, which comprises the track structure and roadbed. The provision made in the accounts in respect of these elements of property, is, what is known as "renewal accounting".

Q. Now, can you say whether the figure of $1,272,000,000 of gross investment represents actual cost or is it more or less than actual cost?

A. It is substantially less than actual cost. Unlike carriers in the United States, our Company since its inception followed the system of renewal equipment for shop and plant machinery and road property up until July 1, 1942. Renewal accounting, I may say, is a system used by English Railways. Under that system when a unit of property is being replaced, that is, torn down, and a new unit erected, no increase in property investment would be recorded on the books to the extent of the renewal in kind even though the current price of labour and materials were in excess of the prices at the time the original structure was built.

Q. Now, can you give the Commission an illustration of what you mean by that?

A. Assume a station was built, a frame station, in 1885, at $25,000 - -

Q. Cost $25,000?

A. Yes, and in 1905, that station was replaced by a brick structure, with some improvements in it over the

old station, at a cost of $40,000.

Q. Then go ahead.

A. And assume that in 1905 - -

Q. That is, when the new one was built?

A. Yes, that the old frame station at that time could be built at a cost of $35,000.

Q. Then, assuming all that, what takes place in the books?

A. The original investment - -

Q. That is $25,000?

A. Remains in the books. The cost of the replacement in kind - -

Q. That is $35,000?

A. Yes, that is charged out to expenses.

Q. Then, what about the difference between the cost of replacement in kind of $35,000 and the cost of the building that you actually put up of $40,000 - that is $5,000?

A. That $5,000, that betterment, is added to the investment account.

Q. Then, would it be true to say, that the new station would be recorded in the books at the original cost plus the betterment, that is $30,000 although it cost $40,000?

A. That is right, that is an understatement of $10,000. That is an understatement of 33 1/3%.

Q. Now, have there been many of those cases?

A. Yes, that system of renewal accounting has applied throughout our history up to July 1, 1942, and would affect all the accounting in respect of property that has been renewed.

Q. I suppose some of these facilities have shorter life, and have been renewed two or three times since they were originally built?

A. Yes, they have been renewed two or three times, in which case, Mr. Evans, the understatement of cost would tend to pyramid.

COMMISSIONER INNIS: Are there any stations which have been built in 1885 still in use?

A. I do not know of any one, but there may be a few, sir. But I know of some stations that have been renewed three times.

THE CHAIRMAN: In that period of years, you mean?

A. Yes, sir.

MR. EVANS: Well then, does this same matter of understatement of cost apply to all fixed assets in the road property of the company?

A. Yes, Mr. Evans,

Q. Is it possible to ascertain the understatement of investment in regard to that practice in connection with road property?

A. Not the sum total of the understatement below actual cost. That is not possible to determine short of an actual complete inventory, but certainly the amount is substantial, Mr. Evans.

MR. McLEAN: This is the $200 million, isn't it?

A. I have not mentioned $200 million.

MR. EVANS: Now then, have you any comments to make in regard to the deduction for depreciation, that is, the figure of $340 million to arrive at the investment basis of $1,001,000,000?

A. Yes, the amount of depreciation deducted from our

investment base of $1,001,000,000 at December 31, 1947, amounted to $340 million. Now, I have set down in my notes here, a tabulation as to how that figure has been built up.

Q. Will you give those please, Mr. Liddy?

A. Well, credits made to the reserve for charges made to working expenses prior to the adoption of depreciation accounting amounted to $54 million.

Q. That is what percentage of the reserve?

A. That is 16% of the reserve.

Q. Next?

A. Secondly, special appropriations from profit and loss and minor adjustments made at and since the time of the adoption of depreciation accounting amounted to $164 million.

Q. That is another round figure?

A. Yes, sir, or 48%.

Q. Now the next?

A. Charges to working expenses less retirals since the adoption of depreciation accounting amounted to $122 million or 36% of the total reserve.

Q. That means that since depreciation accounting and after deducting the returns and the accrual to the reserve, the cost of $122 million or 36% has been met by charges to working expenses?

A. That is right.

Q. And the balance is made up of these appropriations and credits you have spoken of?

A. Yes, sir.

Q. Now, Mr. Liddy, when did the Canadian Pacific undertake depreciation accounting?

A. For inland steamships, depreciation accounting commenced January 1, 1934.

THE CHAIRMAN: When was that?

A. January 1, 1934. For rolling stock January 1, 1940, and for road property July 1, 1942.

MR. EVANS: How about for income tax purposes?

A. For income tax purposes, Mr. Evans, we had records extending back to the year 1920, and in 1948 it was decided to bring the railway depreciation reserves into line with and into agreement with the income tax records.

Q. What was the effect of that?

A. While the Canadian Pacific only commenced depreciation accounting in recent years, the effect of the credits and special appropriations which I have mentioned has produced a depreciation reserve which represents a substantaal proportion of depreciable investment and of gross investment.

Q. Now then, having regard to these statements you have made, and the understatement of investment and low cost, substantial adjustments and transfers to build up the depreciation reserve, what have you to say as to the depreciative book investment base of $1,001,000,000 as of December 31, 1947?

MR. MacPHERSON: That is the very point I have raised before, Mr. Chairman, that there is involved in this, I submit, more than the innocent question that has been asked, and I say that for this reason. I repeat what I have said before, that before the Board of Transport Commissioners my friends sought to establish a rate based on these same figures that he is now putting to the witness, and thought that they had established a rate

bases on which a rate return would be granted. The Board of Transport Commissioners did not accept that, and, as indicated, the Board of Transport Commissioners proceeded on the basis of requirements. We had argued for requirements, not on the basis of the formula that had been used, but we had argued as against the rate base.

Now, the question that has been put to the witness now, is a question which will secure information as to the desirability of establishing a rate basis based entirely on book figures without regard whatever to prudent investment or any of these other ingredients that we submit, and we would argue without entering into the question, that is to say, the question as put, and the answer as received, may very well form the basis for the contention that mere book figures unsubstantiated in any way, mere book figures as produced here would be sufficient to establish a rate basis.

(Page 16640 follows)

MR EVANS: I would like to say this much about it, sir, that mere book figures have been accepted by the Interstate Commerce Commission. They started out on a study of replacement cost, and for many years they went on a replacement cost rate base; they have now gone to a book cost rate base. My friends have referred to our failure to establish prudent investment. Now, my friends very well know that the cases in the United States where that has been very largely discussed make it quite clear that the onus lies on him who suggests that the investment is not prudent to establish that it is not prudent, and that prima facie evidence of a rate base is regularly and usually accepted from the books of the company. Now, I have nothing further to say. If the Commission feels that my friend's objection is sound, I do not---

MR SMITH: May I be allowed to say something at this point, my lord?

THE CHAIRMAN: Yes.

MR SMITH: I think it is a vital point. I do assert very strenuously that the position taken by my friend as to the American practice is not correct. On this question there was evidence adduced in the 20% Case, and also argument by Mr. Priest, an American counsellor, on the question of rate base and the practice of the Interstate Commerce Commission, and it was asserted there that the mere proof of the investment cost as disclosed in the books constituted the minimum rate base, and it was said that that basis was the one established by decisions of the Supreme Court of the United States. I want to assert most strenuously, my lord, that that is not the position of the American courts. The position under the American Constitution, as I read it, is that the amendments to the Constitution provide, in what are known as the due process provi-

sions, that property cannot be taken from a person by legislation of a state without payment, without compensation. So in the case of Smyth v. Ames, which is a case of 1898, the Supreme Court of the United States laid down the rule that in considering the action of a regulatory body of a state the public utility should be entitled to a fair return. Now, there was a great divergence of opinion as to the views expressed in that case in 1898, and the upshot of the decisions in the United States was, in the case of Hope v. Federal Power Commission, in 1944, where the basis of the judgment of the regulatory body in the state was that of original cost based on prudent investment, or, as it was called in the Act, legitimate cost, and the Court decided that a body, a regulatory body, could accept any principle for the basis for fixing a rate base if it was not confiscatory, and in that case there is no approval of accepting a book value as such. The case in the Supreme Court of the United States was not on the question of proof; it was proof by book cost or any other cost. It said that latitude is allowed to the Commission, or to the regulatory body in the States, to accept any method which is not confiscatory.

Now, of course we have not in Canada such a restriction on the power of the legislature as provided in the amendments, which I think are the seventh and the fourteenth amendments to the Constitution dealing with due process. But what was done in that case before the body that dealt with it, the regulatory body in the state before the time of the Interstate Commerce Commission, was that the legitimate cost was taken, and it is true that the starting point was the investment cost as shown by the books, but the evidence shows, by the report in the Interstate Commerce Commission, that there were much more on this

point than the mere book value. This question is dealt with at length in Mr. MacPherson's argument in the 20% Case. But what I do protest against at this time is a statement by railway counsel that they proved a rate base in the 20% Case which would be accepted in the United States. I say that is far from the actual truth.

MR FRAWLEY: My lord, might I address myself to what I think is a practical aspect of this matter? I find nothing in your lordship's Commission which requires you to make any report upon the advisability of railway requirements being satisfied on the basis of a rate of return on a rate base. I find nothing specifically in sub-paragraph (d).

THE CHAIRMAN: We were directed to provide guidance to the Board in their revision of freight rates, for instance, but by legislation.

MR FRAWLEY: "To review the Railway Act with respect to such matters as guidance to the Board in general freight rate revisions, . . ."

What I was going to say was---

THE CHAIRMAN: I think if you go on you will see that it is by way of amendments to legislation.

MR FRAWLEY: " . . . and recommend such amendments therein as may appear to them to be advisable."

What I was going to say, my lord, was, assume that there was a particular directive to the Board to deal with the matter of freight rates; what is the practical---

THE CHAIRMAN: Do you mean the Board?

MR FRAWLEY: Assume that there was a directive, a special directive, to this Commission to consider the matter of rate base as such; I put it to you, my lord, what is the practical value of the kind of evidence which Mr. Evans is now seeking from the witness? I associate myself

wholly with what Mr. Smith has to say, that the railway did not in the 20% Case establish a rate base. We were surprised that they should attempt to do that, having based their case on requirements, but during the case, in any event as it seemed to us, they shifted their ground and they then attempted to prove a rate base. We challenged it, and your lordship will see from the report of the Board that their Exhibit 49-49 was not accepted as a rate base, and the Board says so in just so many words; but that is not---

THE CHAIRMAN: What did the Board say?

MR FRAWLEY: There are two or three paragraphs on rate base and rate of return, and I want to conclude with just one paragraph, where the Board gets to its decision. After reviewing what Exhibit 49-49 said, or what Exhibit 49-49 attempted to say, the Board says:

"Counsel for Saskatchewan has directed attention to the fact that the rate base figure submitted by the Canadian Pacific includes therein items given to the Company by Canada totalling $170,000,000. While this may be counterbalanced by the $200,000,000 understatement of investment as claimed by the railway, yet it indicates to me that the Board cannot accept Exhibit 49-49 for a rate base determination. I am not suggesting that the company's books do not correctly reflect its investment position from a corporate standpoint. There may be advantages in being able to accept the statements of the company and disadvantages, from the standpoint of all parties, in making a rate base determination by other means. However I do not believe that such considerations justify me in determining without further evidence and investigation that the investments have been prudently

made, and that the revenues have been sufficiently accounted for. Notwithstanding, therefore, the very able and learned arguments advanced by counsel for the Canadian Pacific Railway and notwithstanding the evidence of the learned experts, I accept the arguments advanced for the Province of Saskatchewan and the Maritime Transportation Commission that much more evidence than that adduced will be necessary to justify this Board in deciding that from this exhibit and the evidence in its support a rate base had been established for the purposes of dealing with this application."

Now, that was what the Board said about the evidence in the 20% Case, where we spent days and days and weeks on this exhibit. For my friend to come in now and attempt by these few simple questions to establish the rate base is to my mind an untenable position.

But that is not why I got up to address the Commission. I say, my lord, that if the Canadian Pacific Railway wants a rate base, wants a rate of return on its rate base, let them go to the regulatory body and put in what they think is a rate base. We will be there to challenge them.

MR EVANS: You certainly will.

MR FRAWLEY: We will indeed be there to challenge them, to make them show that it was all prudently invested, to make them show that it is there now and used in useful assets; and without those two fundaaental principles there can be no rate base established. So I am merely addressing myself now to the question---

THE CHAIRMAN: You say there can be no rate base established?

MR FRAWLEY: Unless those things are proved;

there can be no rate base established unless those things are proved.

THE CHAIRMAN: What then would you have recourse to as a method?

MR FRAWLEY: They could carry on as they have since 1920; they just prove their requirements -- so much for dividends, so much for fixed charges and so much for surplus. They do now. There is to be a judgment to-morrow that we don't know anything about, but as far as we know they certainly cannot proceed on the basis of a rate base.

But the point I was simply seeking to make now was the futility of this kind of evidence to this Commission. If the Canadian Pacific Railway has decided now, after thirty years, that they want to present their rate increase cases to the Board on a rate base, let them do it. What is the object of coming to this Commission and saying, "We want to establish a rate base"? This Board is not giving them any freight rate increase.

Now, I say that in all seriousness, that we are taking up a lot of time unnecessarily. Let them go to the regulatory body and attempt to prove a rate base. We will be there to see that it is properly put in as far as we can; but it seems to me, sir, that to try to do it now, to try to argue to this Commission now that this is a rate base, is futile. How can this Commission decide any such matter as that? And why does Mr. Evans care? Why does Mr. Evans want to establish his rate base to this Commission? This Commission is not giving him a rate of return on it.

MR MACPHERSON: My lord, there is just one thing I would like to add relative to the American cases that have been cited or referred to by my friend

Mr. Smith. These, of course, are all reported, but when you go particularly to the early decisions, the Hope case, the Natural Pipeline case, you see in what measure the Federal Power Commission in the United States had a whole battery of accountants and engineers and independent experts of their own who went into it most carefully and checked vouchers and accounts and everything else -- a situation that does not exist in similar---

MR EVANS: I will be glad if my friend would give a reference to the case where the Federal Power Commission went in and checked vouchers. I would be very interested in that case.

MR MACPHERSON: I will be very glad to give my friend the information. I haven't it here, but I will be glad to get the information and give it to him.

THE CHAIRMAN: Mr. MacPherson and Mr. Frawley, we must remember that the C.P.R. in its brief at page 64 made a certain statement, which is contained in four paragraphs. They say, to begin with, that they submit that in order that rates be just and reasonable to the railway the general level of rates should be such as to provide an equitable return on the investment in railway property used in transportation service. Now, that is what they are contending for. I won't read all the rest, but in the last of their paragraphs they point out that all this could be done without any amendment to the Act at all; that is, it is open to the Board today if they like to establish that means of fixing freight rates. Then they say if that seems to be the best method of dealing with such cases, the determination of the investment in such property and the rate of return are matters which should properly be left to the Board of Transport Commissioners. Mr. Evans tells us then that the Board can do these things

today without any amendment. You say the Board has not been proceeding on that method so far.

MR FRAWLEY: They have not been proceeding on that.

THE CHAIRMAN: Mr. MacPherson says the same thing. Well, I can only construe, then, the C.P.R.'s request to us is that we do provide by amendments to the Act that this shall be the basis for fixing freight rates in the future.

MR FRAWLEY: That would be a reversal of the statement, surely, on page 64, where it is submitted that no amendment is necessary to the Railway Act to apply the principle.

THE CHAIRMAN: No, no, that is not a reversal. He says today the Board is free, and no amendment is necessary to give the Board this power; the Board has it. But you tell me that the Board has not followed this method. Mr. Evans says the Board---

MR FRAWLEY: Perhaps I should add, there was never any application to the Board on that basis, sir.

THE CHAIRMAN: That may very well be. Now, if I understand Mr. Evans, he means that hereafter the Board should be compelled to follow this method; he wants this method established as the proper one. Am I exaggerating what you are asking?

MR EVANS: Well, I had not asked for any amendment to require the Board---

THE CHAIRMAN: I know you haven't, but you were asking us here to hold that the proper method of establishing a base is the one that you say here.

MR EVANS: Yes.

THE CHAIRMAN: An equitable return on the investment in railway property.

MR EVANS: Yes.

THE CHAIRMAN: Now, that is a method which the Board so far has not followed.

MR EVANS: Well, I would not agree with that statement at all.

THE CHAIRMAN: You say they followed it?

MR EVANS: They have followed it in other cases, yes.

THE CHAIRMAN: Well, it is a very serious state if we cannot have a more definite statement agreed upon, as to a matter which is continually going on before the Board, the method of fixing rates, if we have today, after all these years, one set of counsel saying the Board has followed one method, and another set saying the Board has followed another method.

MR FRAWLEY: Surely that can be settled instantly. The Board of Transport Commissioners may have followed it in telephone cases, in tramway cases -- I don't know -- but not in railway cases.

THE CHAIRMAN: We are talking of railway cases.

MR FRAWLEY: Mr. Evans is not saying that they have ever allowed a rate of return on a rate base in a steam railway case. I say they never have. Mr. Evans is not disagreeing with that.

MR MACPHERSON: There is no disagreement at all.

MR FRAWLEY: There is no disagreement.

THE CHAIRMAN: What do you say now, Mr. Evans?

MR EVANS: I say exactly as I said before, sir, that they have applied the historical cost or investment rate base principle in other cases. I did not say railway cases.

THE CHAIRMAN: Oh, well!

MR EVANS: Ottawa Electric Railway and B. C.

Telephone.

THE CHAIRMAN: You are, then, asking us to recommend that in future they should take your basis?

MR EVANS: I did not ask for that, sir, at all.

THE CHAIRMAN: Well, if you are not asking for anything, you should not have any evidence before us. You must be asking for something.

MR FRAWLEY: That is exactly the point.

MR EVANS: May I have a word?

MR MACPHERSON: That was my reason, seeing, as I thought I saw, where this was leading. That was why I raised the objection at the start.

THE CHAIRMAN: Well, I must take the brief as it is. The brief is there. It has not been challenged as being improperly there so far, and the brief does ask us in four different paragraphs, or allege to us, that the proper way to fix a basis is the one that they set out here, the basis of a fair return on the investment in railway property used in transportation service. Apparently I gather now, Mr. Evans, that that basis has not so far been followed by the Board in railway cases.

MR EVANS: Oh, no, sir.

THE CHAIRMAN: Good. But you think that in the future it ought to be?

MR EVANS: I think so, yes.

THE CHAIRMAN: And you say that no amendment to the Act is required to give the Board power; they have that power. Now, do you want us to go so far as to provide by law that they must follow this basis in future?

MR EVANS: No, sir. May I say what I think the relevancy is?

THE CHAIRMAN: Yes.

MR EVANS: It is not a fundamental part of my

case that this Commission would ask that the Railway Act be amended to provide for this, but I do not think that in any general submission which goes to the root of the transportation problem in this country this Commission could have an understanding of it without knowing this problem of rate of return. It is necessary to understand it in order to determine, for example, what are just and reasonable rates. Now, I am not going to fight with my friends. They are terribly sensitive about this. You would think there was some trouble going to come of it. It is only that if the Commission wants it I am quite prepared to offer it; if the Commission does not want it I have nothing further to say. I thought it would be informative and helpful, and I think it goes to the root of the problem of the railway in this country. My friends shudder and they get to their feet and they shout and they clamour as soon as investment rate is mentioned -- because, I suggest, they are afraid that we are not getting an adequate return and they are afraid that it may cost them a little bit to have that investment base approved.

THE CHAIRMAN: I take it, then, that you now are showing or trying to show that you have the proper material to establish the facts which would make this a proper base.

MR EVANS: Yes. Now may I say one other thing, sir? There has been an awful clamour here. I have not raised objections to the relevance of a lot of the evidence; I could have done so. There has been a terrific clamour about Other Income. Now, this is one way of solving Other Income, and, as you will recall, in some of my cross-examinations, and I think Mr. Covert also elicited in cross-examination admissions from the accounting witnesses for the provinces that if you were going to take in Other Income from these outside other than railway operations, you also

had to take in the investment. Now, if it is fundamental to this Commission's consideration that they should hear from the provinces as to whether Other Income should be excluded or included, then it seems to me it is inevitable that the Commission has to know where that leads you in the matter of railway rates, because if you take in this Other Income without going for a return on the investment represented by the assets that produce that Other Income, then you are going to distort the railway rates downward, and provide no return to the company on the investment in those properties.

Now, I would have thought, and I would most warmly submit, that the Commission would find it informative; if they do not, I have nothing to say.

THE CHAIRMAN: Well, we are about to adjourn now for lunch. In the meantime we can think these things over, and, Mr. Covert, perhaps you will have something to say to us this afternoon.

MR COVERT: Yes.

THE CHAIRMAN: We will not go any further just now. The point, then, is whether this evidence is of any value to the Commission, having regard to the work we have undertaken.

---The Commission adjourned at 1:00 p.m., to meet again at 2:45 p.m.

Tuesday, February 28, 1950.

AFTERNOON SESSION

$. J. W. LIDDY, recalled:

Examination by Mr.Evans resumed

THE CHAIRMAN: Before we proceed, Mr. Evans, is there anything more to be said about the matter which was under discussion before we adjourned? You are going on to give us these figures?

MR. EVANS: I am almost through, Mr. Chairman. I have just a few questions left.

THE CHAIRMAN: Are those objections still being pursued, Mr. MacPherson?

MR. MacPHERSON: The last question that was put was the one to which I objected, and to which I still object.

THE CHAIRMAN: You are referring to some particular question?

MR. MacPHERSON: I refer to the last question which was asked of Mr. Liddy.

THE CHAIRMAN: What was that?

MR. EVANS: It had to do with his comment in regard to what he had said, that is, what was his opinion as to the net depreciated book investment of one billion two million as a rate base. That was the question which was objected to.

THE CHAIRMAN: The situation seems to be this: you have set out there on page 64 your preference for certain base rates with respect to freight rate structure.

MR. EVANS: Yes.

THE CHAIRMAN: And you say, however, that the Board now has full and sufficient power to adopt those bases, if the Board wants to?

MR. EVANS: Yes.

THE CHAIRMAN: We have been told, as we went along, on different occasions, when counsel for one interest said so and so, then counsel for another interest would say: The Board can do this now.

Do you think this is sufficient answer? I thought the purpose was to ask us to recommend that the Railway Act provide for this particular basis to be set up. What of that, if you would leave it all with the Board anyhow?

Mr. Frawley has asked us on several occasions to make recommendations to the Board which the Board might be inclined to adopt. Is that your submission here?

MR. EVANS: No, sir. I am merely being informative. And if the Commission thinks I am not being informative, then I have nothing to say.

THE CHAIRMAN: Well, if you are just being informative, I think the information you are giving us throws a light on the question of rate making, upon uniform accounting, for instance, and as to how your institution does dispose of these things -- and probably the Canadian National does the same thing, I do not know.

But I think this information would be informative to us for our general purposes, and I do not see why it should be excluded, having regard, then, to the fact that Mr. Evans says that he is not asking us to propose any amendment to the law curtailing the present powers of the Board in selecting its own method of erecting a freight rate structure. Is that clear?

MR. FRAWLEY: Then why does my friend want an answer to his question? What is this one billion two? He is still talking about a principle and about the advisability of the rate base method; and I do not think he needs to have an answer with respect to this particular sum of one billion two million.

THE CHAIRMAN: If we were deciding any issue, Mr. Frawley, then I could understand your objection; but we are not. That is not the case. This is not a case in a court.

We are having certain information offered to us. You yourself, Mr. Frawley, have offered us a lot which we were glad to have. But we are not asked to do anything with it.

MR. FRAWLEY: Well then, Mr. Chairman, should it be in the records of this Commission that today a witness established $1 billion 2 million as a rate base for the Canadian Pacific Railway? I say it should not.

THE CHAIRMAN: We are not taking it as establishing anything at all.

MR. FRAWLEY: But that is just what Mr. Evans is doing. He is establishing 1 billion 2 million as his rate base.

THE CHAIRMAN: Not at all. Do you mean to say that Mr. Evans could go next week and establish his rate base by simply referring back to what he did here today?

MR. FRAWLEY: Oh no, he could not do it. But I do not know what he might do.

THE CHAIRMAN: What is being said both by you and Mr. Evans and by myself is all going into the record. We are just taking these figures in an informative way for what they are, and we do not consider that they are establishing anything in particular.

MR. FRAWLEY: This witness is saying now -- or will now say in a moment if he is allowed to: this is an established rate base.

THE CHAIRMAN: He says this is what they put forward and think an established rate base ought to be. But that does not establish anything.

MR. FRAWLEY: Of course it does not.

THE CHAIRMAN: But subject to that --

MR. FRAWLEY: I submit that we must have time to meet the proposition, if we are going into a rate base of $1 billion 2 million, and that we should have the opportunity to bring in witnesses.

THE CHAIRMAN: What would you argue for?

MR. FRAWLEY: That a lot of things have not been proved by simply offering the balance sheet of the Canadian Pacific Railway Company.

THE CHAIRMAN: That is quite right; and as I have told you, we are taking all subject to that; that is, we are not taking these figures as proving anything.

MR. FRAWLEY: Anything?

THE CHAIRMAN: No.

MR. FRAWLEY: Then why offer them, even?

THE CHAIRMAN: They would be informative to us because they would show how the Canadian Pacific does its accounting.

MR. FRAWLEY: Oh no, not this figure. Rather, how it calculates its rate base.

THE CHAIRMAN: Yes; but it does not establish anything; that is the way I look at it.

MR. MacPHERSON: My lord, merely for the purpose of being informed I would like to quote to your lordship and to the Commission from 264 I.C.C. at page 723, from a case that has been cited before. It is Ex Parte 162.

THE CHAIRMAN: Remember now you are dealing with the decision of a body which had to adjudicate in these matters. What did they have to say?

MR. MacPHERSON:

"As we said in St. Paul and Puget Sound Accounts, 29 I.C.C. 508, 509 -

all students of railroad economics are well aware of the fact that, prior to 1907, when the Commission was given real power to control such matters, the accounts of carriers in many cases were influenced more by other considerations than by a desire to reflect the actual facts.

And in our annual report to Congress for 1908, we referred to -

the well-known facts that no court, no commission, or accountant, or financial writer would for a moment consider that the present balance sheet statement purporting to give the 'cost of property' suggests, even in a remote degree, a reliable measure either of the money invested or of present value."

THE CHAIRMAN: You are putting that on the record. There it is.

MR. MacPHERSON: And the judgment then goes on to say:

"Since adoption and use of the prescribed uniform system of accounts the force of these criticisms has been lessened, particularly as to property acquired or constructed after 1907, but as to the older portions of the railroad properties, the criticism remains valid to a considerable degree."

THE CHAIRMAN: Has anybody else anything to say?

(Page 16660 follows)

MR. EVANS: Well, I was going to say I have only two or three more questions, and I am quite content to leave it.

THE CHAIRMAN: Would you care to say anything, Mr. Covert?

MR. COVERT: Well, my lord, it seems to me one of the principal considerations that the Commission has to consider is whether or not they would determine a rate base, and it semms to me that the answer to that, I submit, would probably be no.

THE CHAIRMAN: We are not being asked to determine a rate base.

MR. COVERT: No, and the second thing it would seem to me, Mr. Chairman, is that you must be interested in the disuussion of the principle. I would think you would be, and I think there probably should be a full discussion of that principle. Whether or not we receive figures and how much time we spend on receiving figures, would depend on whether or not they would be informative as Mr. Evans said; I would use the word exemplary. Perhaps they might want to use these figures to show as an example what would happen, what would be the difference if a rate base was used and if they went on the basis that they have been in the past of financial requirements.

I think all these things are of interest to the Commission, and especially if there are only two or three more questions, it would be better to spend more time in this way, and the Commission can do as it feels.

THE CHAIRMAN: Well, I think you had better go on, Mr. Evans. If we find it necessary to deal with this question in a report, we would be at pains to point these

things out.

MR. EVANS: If I were trying to establish a rate base today, I would not be using 1947 figures. I am merely putting this forward to establish the principle, and I would like to refer the Commission, since my friends have been so active in this matter, to the argument of Mr. A. J. G. Priest, in the 20 Percent Case. Now, the whole issue, as far as rate base and returns can be found in that argument. In my respectful submission it is an artistic and complete and very clear exposition of the whole principle. It reviews the United States cases, and my friends can say that I have mistated it, but the cases are there and they are discussed, and I should like to give the Commission a reference to that argument. It begins at page 3959 of the Transcript in the 20 Percent Case, and it ends at page 4035. There is about 80 pages of this in the argument in chief, and in reply even less, page 4680 to page 4705. It is really quite short, but there is the law as Mr. Priest presented it to the Board, and the cases are referred to and what the cases decided, and, as far as I am concerned, I am quite content to leave the subject.

MR. MacPHERSON: My lord, I think Mr. Evans has given you the citation as to Mr. Priest's argument on this, and probably, while it is a much inferior argument, I might give a reference to my own argument in reply which will be found in the same 20 Percent Case from page 4536 on, and it deals with the problem as we saw/it from the provinces, and I need only add, that the view that we submitted in that connection was, as has already been indicated, accepted by the Board of Transport Commissioners on the argument.

MR. EVANS: I would say no, because you made the suggestion, that you could not have a rate base without an

estimate of value or at least Mr. Smith did.

MR. SMITH: That is not correct - unequivocably not correct.

THE CHAIRMAN: Well, I want to assure you all that your guns are carrying blank cartridges just now.

MR. EVANS: I will go on with another subject, if your lordship pleases. Mr. Liddy, at page 109 of the Canadian Pacific Submission, I am going to read paragraph 56 of the outline submission:-

> "There is already a substantial degree of uniformity in accounting methods and statistical procedure as between Canadian National and Canadian Pacific. Both companies adhere closely to the accounting classification of the Interstate Commerce Commission. As provided for in the Railway Act and in the Statistics Act, the railways in Canada submit annual reports, on prescribed forms, to the Board of Transport Commissioners and the Dominion Bureau of Statistics, furnishing details of their accounts and statistics of their operations. Many periodic and other reports are also submitted to the Board and to the Bureau."

Now, Mr. Liddy, what is your view as to whether uniformity in accounting for Canadian railways can be achieved?

A. Since there is already a considerable degree of uniformity existing, I believe the obstacles to complete uniformity in accounting and statistical procedure could be overcome in a reasonable time or largely overcome to the extent warranted. There are some difficulties and some differences of opinion, but the advantages of a uniform

procedure are, in my view, worth the time and effort to achieve. It will be realized, of course, that whatever the degree of uniformity which may be achieved in accounting, there will always remain fundamental differences between railways which preclude exact comparisons being made.

Q. What, in your opinion, would be the first step towards obtaining uniformity in accounting?

A. I think the first step is to adopt a uniform classification suitable for Canadian railways.

Q. What general considerations would you think should be applied in adopting that uniform classification?

A. First, I believe the classification should be designed to show the financial result of conducting railway transportation as is prescribed for United States railways by the Interstate Commerce Commission.

Q. Anything else?

A. Yes, I believe the Canadian classification should follow the same principles of accounting as are embodied in the Interstate Commerce Commission classification, and that depreciation accounting should be applied to the same classes of property in Canada as are prescribed for United States carriers.

Q. Now, what else have you to say on that?

A. I believe the details of the classification should be designed to permit ready comparisons of significant primary accounts being made between Canadian and United States railroads.

Q. Could there be any simplification in your view?

A. Yes, I believe the same simple classification of accounts should be attempted for use in Canada that presently prevails for Class 1 carriers in the United States.

Q. Can you say why you believe that?

A. The incidence of a large number of individual accounts means, in many instances, that payroll and material charges are required to be analyzed minutely in order to segregate the charges for the requirements of such a classification. This requires not only the work of clerks in the accounting offices, but also much time of railway employees out on the lines in filling out forms. The simplification to be attempted, however, should in my view, not go beyond consolidating all individual Interstate Commerce Commission primary accounts and only when worthwhile results can be achieved.

Q. Now, we have been talking before about the segregation of passenger and freight accounts. Have you anything to say in this connection on uniformity about that question?

A. Yes, I consider the Interstate Commerce Commission practice of requiring carriers to keep segregated freight and passenger accounts, is , in my view, an unnecessary requirement for Canadian railways.

Q. Are there any other considerations that you think should be borne in mind in discussing this question of uniform classifications?

A. I believe one single classification of accounts in Canada should be prescribed for all Canadian railways rather than the separate or condensed classifications which are in effect for the smaller railways in the United States.

THE CHAIRMAN: Would you pardon me a moment? Does what you are suggesting now, mean, a departure from present practice in Canada, because, you see, that paragraph in the Brief says that "Both companies adhere closely to the accounting classification of the Interstate Commerce Commission"?

that is what is going on now?

A. Yes, sir.

Q. You seem to think that ought to be changed?

A. We have not got equal uniformity in accounting in Canada.

Q. Well, the Brief says that there is "a substantial degree"?

A. That is right.

Q. And then it goes on to say that both companies adhere closely to the accounting classification of the Interstate Commerce Commission?

A. Yes, sir.

Q. Now, bearing those two statements in mind, what have you to say?

A. Well, I would like to bring the "closely" a little closer, sir. If that were done, I think we could achieve a greater degree of uniformity in Canada without hurting anyone .

Q. You mean closer to the Interstate Commerce Commission? That is where the word "closely" is used - "both companies adhere closely to the accounting classification of the Interstate Commerce Commission"?

A. Yes.

Q. I thought you said a little while ago that there are certain portions of that system which you think it is not desirable to adopt in Canada?

A. Not in respect of the classification, sir, except I think it is perhaps a little too elaborate for Canada, but in respect of the principles of the Interstate Commerce Commission classifications, I think they are sound. They have been developed in that country since regulation started.

I am in the hands of counsel, but I think it goes away back to 1888, and there has been the advantage that it has been reviewed by a large number of railways and the Interstate Commerce Commission and a lot of State Commissions so that I would urge that the principles of accounting of the Interstate Commerce Commission classification be not departed from if at all possible.

Q. But that is only in regard to classification?

A. Well "classification" includes principles.

Q. It is a great deal of the whole problem?

A. Yes, sir.

Q. Now, may I ask you - I think this would be a useful time to ask it - having regard to that paragraph (d) of Section 2 of the Order-in-Council it would be well to know now whether we can expect any contention on that. We are asked to review the present-day accounting methods (that is what we are doing now) and the statistical procedure of the railways in Canada, and to report upon the advisability of adopting measures conducive to uniformity in such accounts. So far, it seems to me that everybody has been favourable to the principle of uniformity in accounting. Is that right, or am I wrong there?

MR. MacPHERSON: That is correct.

THE CHAIRMAN: Then, go on, Mr. Evans.

(Page 16668 follows)

MR EVANS: Well, I might just say this, that, as your lordship will remember, we rather point in the brief to the danger of thinking that you are going to get the kind of complete comparability in theresults merely by uniform accounting. I think we point that out, but in principle we are not opposed in any way to uniform accounting. But there are some qualifications to the detail that I am going to ask the witness about now, that may be helpful.

THE CHAIRMAN: May I ask, then, is the Canadian National also agreeable to the uniform accounting principle? Is that so?

MR O'DONNELL: Yes, we are, my lord, and I think we can even---

THE CHAIRMAN: I am not talking about details.

MR O'DONNELL: No, no. I think we go a little further, though, than our friends do, and our submission is quite detailed in the brief.

THE CHAIRMAN: All right. Go on, Mr. Evans.

MR EVANS: I might say that I thought perhaps when your lordship began to discuss this subject you intended to ask me to say whether I thought the Railway Act required amendment.

THE CHAIRMAN: No. That may turn up later.

MR EVANS: I am prepared to discuss that at any time.

Q. Now, in the general considerations in regard to Canadian classification of accounts, I suppose the subject of depreciation has been mentioned; would you like to elaborate on the subject of depreciation in connection with the uniform classification?

A. Yes. I think, in view of the advantages of the user method of depreciation, and of the overwhelming weight

of expert opinion given in evidence in the recent rate cases in support of that method, if this Commission feels--

MR MCLEAN: I do not think the witness has any right to argue. This is argument.

THE CHAIRMAN: Well, the witness talks about the overwhelming weight of evidence; of course, you can cross-examine about that.

MR EVANS: There is a great disposition today, my lord, to find my friends in a sort of claque behind us, laughing and joking and passing remarks. I do not usually react to those things, but I think there is a limit. I think I have been very much more patient than my friends with interjections.

THE CHAIRMAN: Go on, Mr. Evans.

MR EVANS: Q. You were going to elaborate on the aspect of depreciation in connection with uniform classification?

A. Yes. I was saying that if this Commission feels that it should make any recommendation as to the method of depreciation to be followed by Canadian railways, it should recommend either that the user method be adopted or that any Canadian railway should have the option of adopting that method.

Q. Now, when Mr. Kent of British Columbia was giving his evidence there was some implication that the user basis of depreciation rather tended to reflect replacement cost, although he did say in his cross-examination that it did not necessarily involve any element of replacement cost. Now, what comment have you to make as to whether the user basis does or does not involve elements of replacement cost?

A. I cannot see where there should be any room for doubt on this point. Throughout the recent freight rate cases it was explained many times that our user basis of

depreciation only provided and was only designed to provide for the recovery of the cost less salvage of assets being depreciated. Many exhibits also were submitted testing our user rates on this basis, and on Exhibit 144 in the 21% Case, in reply to a questionnaire of the Board, it was clearly stated that the first factor in the calculations was that the cost of the assets included in each of the various classes of depreciable property was determined.

MR EVANS: The Commission will find references to the evidence, if they desire it, in volume 746, pages 3363 -- that is before the Board -- 3375, 3376 and 3383, volume 747 at pages 3470, 3471, 3474 and 3520, and volume 749 at page 4163, on that question.

Q. Now, have there been any recent developments in respect of depreciation in the railroad field, Mr. Liddy?

A. Yes. The Interstate Commerce Commission has recently been considering the adoption of depreciation accounting for assets presently classified as non-depreciable, such as ties, rails and other track material. They have now issued a proposed order which has been circulated to the railroads for consideration. In this order the Commission states -- and I quote:

> "The depreciation charges for ties, rails and other track material might be based either on the straight line method or on some basis made to correspond with units of use rather than time."

I point to the fact that this order shows that the Interstate Commerce Commission is interested in the user method of depreciation for the items of road property to which I have referred.

MR FRAWLEY: Could Mr. Liddy give us the number of that order?

THE CHAIRMAN: You refer to certain items -- ties,

rails and so on, which I understand hitherto have not been considered depreciable.

MR EVANS: Yes.

THE CHAIRMAN: Have they been so considered in the United States?

MR EVANS: They have been on renewal accounting there, the same as they are here, and in this tentative order -- it is not a final order -- the Commission has invited the railways to express their views on the question of depreciation accounting for these assets. I think we are going to file a copy of that.

Q. You were intending to file a copy of that order, were you not?

A. Yes, we will file one in the course---

Q. Yes; you are going to discuss it for a minute?

A. Yes, sir.

THE CHAIRMAN: By the way, have the railways expressed any opinions on this order?

MR EVANS: Q. Mr. Liddy, do you know whether they have expressed any views on this order?

A. Well, it is now circulated for the railways to discuss, and the procedure with the Interstate Commerce Commission is that after such proposed orders have had a chance to get out and be considered they form a committee and then they interview the Interstate Commerce Commission officers and they discuss the pros and cons, and they may find that this order is acceptable. Now, heretofore I might say that this question of depreciation of ties and rails and other track material has come up, but the railways' chief objection---

THE CHAIRMAN: Q. Has come up in Canada?

A. No; in the United States.

Q. All r ight.

A. The chief objection to it, sir, has been that the railways did not feel that straight line depreciation was realistic in respect of the renewal of ties and rails, and did not put their income account on a realistic basis. To have in a tremendous period of traffic volume the same expenditure appearing in the income account as for another year in which traffic volume was in the depths say of the depression, was entirely unreal and unrealistic. Now, the Interstate Commerce Commission have shown a willingness in this proposed order to look at this situation from the point of view of an index that will reflect the volume of traffic moving up and down, and I cannot say what the reaction of the railways is going to be at this stage, but---

Q. It is too early yet?

A. Too early yet, yes, sir.

COMMISSIONER ANGUS: Q. Are any other parties ordinarily included in these discussions? Does the Interstate Commerce Commission discuss the proposals with the public or the state governments, for instance?

A. I think some of the discussions are quite wide. A lot of these subjects are discussed even in an open forum at some of the conventions, where almost anybody can come. Personally my knowledge of that phase is limited, sir. Our Comptroller was President of the American Railway Association, Accounting Officers Branch, two or three years ago, and he has been the one who has kept in touch with matters of this kind.

MR EVANS: I would have no doubt that if somebody asked to be heard on this question the Interstate Commerce Commission would hear him. I have no doubt of that at all, but I do not know of any actual case.

Q. Now, on this uniform classification, would you give really a summary of your views, Mr. Liddy?

. I believe the Canadian classification should, first, be designed for conditions in Canada; secondly, it should be such as to attain uniformity in accounting to the extent possible for trailway transportation services; and, thirdly, it should permit ready comparisons to be made with similar operations existing in the United States.

Q. Now, have you any views as to how we can progress this matter, bring it forward?

A. I would think, subject to the recommendations of this Commission on the broad principles to be followed, that the classification should be developed under the authority of the Board of Transport Commissioners. In the United States, as I said a few minutes ago, the Interstate Commerce Commission and the railway accounting officers have got together over the years, and the existing classification is a reflection of the views of the Commission and of the railway accounting officers. I believe a similar procedure should be followed in Canada.

Q. What you are saying there is that it needs the combined experience of railway officers and the experience of the regulatory tribunal to decide on what should or should not go into this uniform classification?

A. That is exactly what I am saying, sir.

Q. Now I would like to pass for a moment to the question of the express business in relation to accounting. I understand that in the United States no railway company is engaged in express business, and I also understand that the express business is conducted by what is known as the Railway Express Agency, and that money orders, travellers' cheques and those activities are handled by the American Express Company. Do you know if there is any separate classification of accounts for such companies?

A. Yes, there is a separate classification in the

United States for express companies. I was not able to obtain any extra copies, but I have my own with me. This classification is entitled "Uniform System of Accounts for Express Companies, Prescribed by the Interstate Commerce Commission in accordance with section 20 of the Act to Regulate Commerce."

Q. When was it effective?

A. This classification was effective in 1914 -- July 1, 1914.

Q. Now, about communication services, is there a separate classification for that in the United States?

A. Yes, there is a separate classification. Such companies report to the Federal Communication Commission, and I have a few copies---

THE CHAIRMAN: Q. You are filing this as an exhibit?

A. Yes.

MR EVANS: Exhibit 184, if your lordship pleases. Unfortunately we have not too many copies. Nothing really turns on it; it is merely informative.

---EXHIBIT 184: Uniform System of Accounts for Express Companies, prescribed by the I.C.C. in accordance with sec.20 of the Act to Regulate Commerce.

MR EVANS: Q. While we are on the subject of communications, what are the important companies that are engaged in commercial communications operations in the United States?

A. For many years two large communication systems handled practically all the business in that country. These were the Postal Telegraphs, Incorporated, and Western Union Telgraph Company.

Q. They were merged, were they not?

A. Yes, they were merged about six years ago; in

1943, as a matter of fact, they were---

Q. What is the gross revenue reported by that merged company in 1947, just to give an example of the business done?

A. $207,000,000 was the gross revenue of that merged company.

Q. Now, have you any knowledge as to what extent, if any, the accounts of the United States railways reflect commercial communications' revenue?

A. Yes, I have. In 1947 the total railway operating revenues of all class 1 line haul railways in the United States were $8,685,000,000.

Q. And what proportion of that---

A. Of which only $3,000,000 pertained to telegraph and telephone revenue. By the way, Mr. Evans, that is, 3/100 of one per cent of the railway accounts represent telegraph and telephone revenue.

Q. How does that in significance compare with the gross revenue of the communications company from commercial telegraphs?

.. The significance of telegraph and telephone revenue as a factor in United States railway accounts may be judged by comparing the $3,000,000 with the gross revenue of $207,000,000 for the Western Union.

Q. Now, coming to the Canadian side of the border for a moment, does the Canadian Pacific Express Company file a separate annual report with the Board of Transport Commissioners and the Dominion Bureau of Statistics?

A. Yes, it does. All companies doing express business in Canada are required to do so. These reports to the Dominion Bureau of Statistics and to the Board of Transport Commissioners in turn form the basis for the annual publication which is issued by the Dominion Govern-

ment.

Q. Have you a copy of that?

A. Yes. I would like to file this as an exhibit.

MR EVANS: That is Exhibit 185.

EXHIBIT 185: Express Statistics for 1948 (Dominion Bureau of Statistics).

THE CHAIRMAN: What is Exhibit 185?

MR EVANS: Exhibit 185 is, Government of Canada, Express Statistics for 1948; that is a publication of the Dominion Bureau of Statistics. What the witness has said is that these reports that are made---

THE CHAIRMAN: You say express?

MR EVANS: Express, yes. The reports that are made by the express company form the basis on which this report is founded.

THE CHAIRMAN: For what year?

MR EVANS: The one I am filing is 1948. It is only to show the nature of the material filed with the Bureau and the Board.

(Page 16678 follows)

Now then, does the Canadian Pacific file a separate report for its communications services?

A. Yes. It files a separate report with the Board and with the Dominion Bureau of Statistics.

In the case of telegraph companies, the Dominion Bureau of Statistics also issues an annual publication.

I have here, for the purposes of filing as an exhibit, a copy of the latest issue. It is entitled, "Telegraph and Cable Statistics for 1948."

Q. That is also a Dominion Bureau of Statistics publication?

A. Yes. sir.

MR. EVANS: That will be Exhibit 186.

EXHIBIT 186:	Filed by : Mr. Evans:	Copy of - Telegraph and Cable Statistics for 1948.

THE CHAIRMAN: What is it?

MR. EVANS: Exhibit 186 is a Dominion Bureau of Statistics publication entitled, "Telegraph and Cable Statistics for 1948."

THE CHAIRMAN: Just telegraph and cable?

MR. EVANS: Yes.

MR. EVANS: Q. Now then, in view of what you have said as to the practice of having, in the United States, a different classification of accounts, and the practice in Canada of having separate reports for express companies and communications and telegraph companies, what comment have you to make as to the proposals which have been made to this Commission in regard to the integration in the railway accounts of the activities of the express company and the communications department of the Canadian Pacific?

A. I do not think it is either necessary or desirable. In fact, I would be strongly opposed to it.

Q. And could you tell the Commission why?

THE CHAIRMAN: Strongly opposed to what?

MR. EVANS: Opposed to the integration in the railway accounts of the activities of the express company and the communications department of the Canadian Pacific; and the witness has just said that he would be strongly opposed to it.

THE CHAIRMAN: Yes.

THE WITNESS: I take that position mainly because integration of these services in the railway accounts would only present unnecessary complications.

MR. EVANS: Yes?

A. And I take that position also because telegraph rates and express rates bear no necessary relationship to freight and passenger rates.

For example, in questions relating to the proper level of telegraph rates, one would take into account the investment in communication facilities and the revenues and expenses of conducting communication services.

Q. Is that also true of express services?

A. Yes. In the case of the express company, investment in facilities, and the revenue and expenses in connection with conducting express services need to be separated in determining the level of express rates.

So far as the carriage of express on the railway is concerned, as the accounts are now kept, there is a very simple arrangement under the contract with the express company.

Q. Yes, and what is that arrangement?

A. The express company pays to the railway company the amount of its net revenue from express traffic for the privilege of having its express carried on the railway.

If the entire operations of the express company were integrated with the railway company's accounts, it

would become necessary, in determining adjustments in the level of either express rates or freight and passenger rates, to separate these in some way, as they are now separated. In the result, nothing would be gained by integration of these accounts, and a lot of new complications would come into being.

COMMISSIONER INNIS: Do all the returns from these services go into "other income"?

MR. EVANS: No. The express revenue, as the witness has just said, from the carriage of express, after payment of expenses of the express company within its organization, is paid to the railway, and is reflected in the railway accounts.

MR. EVANS: Q. Perhaps Mr. Liddy would go on and explain what happens to the balance of any revenue which the express company gets.

A. In answer to Dr. Innis, I would refer to the Canadian Pacific Express Company for the year 1948, and to the figures which are contained in exhibit 185.

The Canadian Pacific Express Company had gross revenue from operation of $21,800,000 odd.

Q. What page does that appear on?

A. That is page 2 of Exhibit 185.

Q. Yes. That is the figure at the bottom of the second column, $21,802,824?

A. That is right.

Now, the express company paid to the railway $7,716,000 odd in order to have its express parcels, and so forth, carried over the railway.

Q. Is that the figure in Table 3, Income Account, second item?

A. That is right.

Q. That is the second item in Table 3, $7,716,254?

A. Yes. And now, after having made that payment to the railway, the Canadian Pacific Express Company had left over the sum of $14,086,000; and it had operating expenses of $13,825,000; that is, a ratio of operating expenses to revenue of 98.1 per cent.

Q. Is that 98.1 per cent correct in relation to $14 million of revenue, or have I missed something?

A. No. The relationship is $14 million odd to $13 million odd.

Q. I am sorry, yes.

A. The $7 million is already in the railway account.

Q. I see, yes. That is, the ratio of operating expenses to operating revenues -- those are the two items under that heading in the second column of Table 3; and the ratio is 98.1 per cent?

A. 98.1 per cent is the ratio.

COMMISSIONER INNIS: Q. You probably will remember in the "Life of Van Horne", he refers to the beginning of this policy; and the first question he asked, when he became manager, was: What has been done with these side issues? And they pointed out that they were still in the hands of the railroad. And then he said that in the United States the cream had been taken off, and they had to get along there with the skimmed milk.

I suppose his policy of reserving the cream is reflected in the railway account?

A. Yes, and the fact that the express company pays to the railway all its net brings into the railway accounts all the cream that there is available.

Q. And the same would be true of your Pullmans?

A. That is right. We operate our own sleeping cars.

mrMR. EVANS: Q. Perhaps there is this distinction. I am sure the witness will correct me if I am

wrong.

In the case of the express company, it is a separate corporation. But in the case of the sleeping cars, it is a separate department of the railway.

COMMISSIONER INNIS: Q. And in the United States, would it be a separate thing?

MR. EVANS: That is not true now. I understand that the Federal Government brought an action under their combines legislation in the United States and divided the pullman company, and made them deprive themselves of certain interests. The result is that today, as I understand it, a great many railway companies have bought their own cars and operate their own services.

MR. EVANS: Q. Do you know about that, Mr. Liddy?

A. No, not in any particular detail.

COMMISSIONER ANGUS: Q. The express company pays to the railway $7,716,254. Is that as a result of shipping their things at ordinary rates?

A. No, sir. That is all the net they have.

If you will look at the figures on Exhibit 185, you will see that after paying $7,700,000 odd, and meeting their expenses, and after taking into consideration some earnings they had from financial paper and other operations, they come down to the end result, that it tapers off to near zero.

Q. I understand that. But how is the amount of $7,716,254 determined?

A. That is determined by the express company keeping a separate transportation department, whereby they turn over all of the net of that transportation department after they have met their expenses.

Q. Oh yes.

MR. EVANS: Q. To clear this up: the express

company has other sources of revenue.

I know that you are not the accounting officer for the express company, Mr. Liddy, but perhaps you could tell us what those other sources are, and how they are treated in the accounts?

A. They have some revenue from financial paper operations, such as money orders, C.O.D. orders; and they carry on cartage operations.

In addition, they have some small investments of their own which bring them in a small amount of income; and they also own some Canadian Pacific Railway Company stock.

Q. And what happens to the earnings from those sources?

A. The earnings from those sources are not taken into the Canadian Pacific Railway accounts, because they are not railway operation; but they are taken into our "other income", either in the form of direct payments, or in the form of dividends or disbursements to the Canadian Pacific Railway.

Q. Yes. Now, turning to page 116 of Part I of the brief, we again return to this matter of the order of the Interstate Commerce Commission; and the paragraph which I want to read --

THE CHAIRMAN: You say page 116?

MR. EVANS: Yes.

THE CHAIRMAN: Whereabouts is it?

MR. EVANS: It is the middle paragraph between the two single-spaced paragraphs of the outline submission. And I read:

"Recently the Interstate Commerce Commission and the railroads have commenced studying the matter of applying depreciation accounting to track structure

and the Commission's Bureau of Accounts has proposed that consideration be given to the 'production' (or 'user') method of accruing such depreciation."

THE CHAIRMAN: That is what we heard about before.

MR. EVANS: Yes, that is what we heard about before; and I was going to ask Mr. Liddy if he would be able to file a copy of that order of the Interstate Commerce Commission?

THE WITNESS: Yes. I have copies, Mr. Evans. That is a proposed order.

MR. EVANS: Q. Yes, a proposed order. This is a photostatic copy, is it?

A. Yes. This is a photostatic copy.

MR. EVANS: Yes. And this will be Exhibit No. 187.

EXHIBIT No. 187:	Filed by : Mr. Evans:	Photostatic copy of proposed order of Interstate Commerce Commission.

MR. EVANS: Q. Do you consider that the track elements of ties, rails, and other track material which are covered by that order are subject to depreciation?

A. Yes. They do depreciate.

Q. Would you have any objection to applying depreciation accounting to these items, if the United States carriers were to adopt it?

A. No. I would have no objection, provided there was a sound method developed for carrying it out.

Q. Yes?

A. My own view is that depreciation, allocated on the basis of use, would be a sound method.

THE CHAIRMAN: That would be a second step?

MR. EVANS: Yes.

THE CHAIRMAN: I think you based your question

on "if the United States railways adopt it"?

MR. EVANS: Yes.

THE CHAIRMAN: But suppose they do not. What would be your view?

MR. EVANS: Q. Perhaps Mr. Liddy might answer that question?

A. I think in Canada there is a great deal to be said for keeping a fair comparability as to accounting between the Canadian and the United States railroads.

Q. You would not want to have depreciation of assets in Canada which was not applicable in the United States?

A. That is right.

THE CHAIRMAN: All right.

MR. EVANS: Q. I want to read quite a few pages of the following submission before I ask you about it. I shall begin to read at page 116, as follows:

"OUTLINE SUBMISSION

'60. One of the principal objects of a depreciation system is to charge currently against income an appropriate proportion of the cost of property and equipment used in producing transportation service. The user method, by directly relating the depreciation charge to the use made of the property and equipment, achieves this object. The resulting net income in periods both of high and of low traffic volume is in the opinion of Canadian Pacific more realistically stated than if the straight line method were used.'"

And then there is a paragraph referring to the definition of the American Institute of Accountants. I shall read it although it has been read before. It reads this way, and it appears on page 117:

"'Depreciation accounting is a system of accounting which aims to distribute the cost or other basic value of tangible capital assets, less salvage, (if any) over the estimated useful life of the unit (which may be a group of assets) in a systematic and rational manner. It is a process of allocation, not of valuation. Depreciation for the year is the portion of the total charge under such a system that is allocated to the year. Although the allocation may properly take into account occurrences during the year, it is not intended to be a measurement of the effect of all such occurrences.'

During the recent hearings before the Board of Transport Commissioners in the 21% Case, the foregoing definition was placed in evidence by Mr. J. Grant Glassco, partner in the well-known firm of Clarkson, Gordon and Company, an auditor of the Bank of Canada and the Industrial Development Bank, whose outstanding position in the Canadian Accounting field is widely recognized. There is a clear distinction made in it between the accounting process of allocating accruals to a particular year and the physical fact of depreciation itself.

Canadian Pacific submits that the 'user' method, by directly relating the depreciation charge to the use made of the property and equipment, is ' a systematic and rational' method of allocation.
Mr. Kent, accounting witness for British Columbia, agreed that both the user method and the straight line method complied with the above definition. (See transcript of 20% Case, p. 3222). Mr. Kent previously at pages 3220-1 had accepted the definition put

forward by Mr. Glassco.

The resulting net income in periods both of high and of low traffic volume is, in the opinion of Canadian Pacific more realistically stated than if the straight-line method were used. In this regard, while the Interstate Commerce Commission has so far prescribed the 'straight-line' depreciation method for United States roads, it is informative to note some of the considerations involved in formulating its decision, set forth in its report, dated July 28, 1931, (No. 15100 Depreciation Charges of Steam Railroad Companies - 177 I.C.C. 351), as follows:

P. 413 - 'The straight-line method has the merit of simplicity and ease of practical application and that is no doubt why it has so generally been used.'

P. 414 - 'Where use is the controlling factor, it would be theoretically correct to measure depreciation in units of use rather than time. However, measurement in units of time may be sufficiently accurate unless there is marked instability in conditions of use.'

P. 432 - 'In findings 2 and 3, service life and depreciation charges have been defined in terms of time rather than use. As has been indicated in the prior general discussion, however, if the carriers can develop a practicable plan in the case of any class of property for measuring depreciation in units of use rather than time, the opportunity should be open to present such a plan to us for approval. Findings 2 and 3, therefore, should not be construed to deny this opportunity.'

There is no doubt that the finding of a 'user' formula uniformly applicable to several hundred railroads, operating under varying conditions, would have complicated the Commission's task and delayed its findings and that it took the most practical course available.

(Page 16694 follows)

"Significantly, however, its decision was made without prejudice to a 'user' formula being submitted for approval on a subsequent occasion".

THE CHAIRMAN: You see, there, Mr. Evans, the Commission says that:-

"...if the carriers can develop a practicable plan in the case of any class of property..." ?

MR. EVANS: Yes.

THE CHAIRMAN: I was wondering the other day, if you remember, whether it would not be feasible or advisable to divide railway property into two classes, the one to be dealt with on the user method and the other on the plan method. I wonder if the Commission had something of that kind in mind?

MR. EVANS: I think that is probably what the Commission had in mind. I think our own plan of the user method is applicable throughout, but there are inevitably assets that do lend themselves because of the physical depreciation corresponding to use to a greater degree than do others. Our submission will be in due course, that one need not tie oneself to an attempt to measure depreciation from year to year. That is something that does occur, but it is an accounting allocation, as the definition indicates, and in due course, I will develop that.

THE CHAIRMAN: All right, go on.

MR. EVANS: Paragraph 61 of the outline submission - -

THE CHAIRMAN: Did you intend to go back to something?

MR. EVANS: No, sir, I wanted to distinguish

between sections I am reading. I hope you did not think I was inferring that you had interrupted me?

THE CHAIRMAN: No, I thought myself I had diverted you from your route.

MR. EVANS: No. Paragraph 61 of the outline submission:-

> "61. The user basis of depreciation is particularly suitable for railway operations because the volume of railway traffic and accordingly the use of railway property fluctuates more violently than in the case of other public utilities. Appropriate statistical measures of the use of railway equipment and property are available. This method has substantial advantages, not only to the railway company, but also to the users of railway service and tends towards a stabilization of railway employment.
>
> 62. If, notwithstanding the position taken by Canadian Pacific in Paragraphs 26 and 27 of this submission, your Commission should feel that it is required to study the matter of depreciation, Canadian Pacific submits that the evidence presented in the proceedings before the Board of Transport Commissioners in the recent freight rates cases, together with the argument of counsel on the subject, should be taken as part of the record in your proceedings in order to avoid the expense and delay which would be occasioned by duplicating such evidence and argument before your Commission".

And I go to page 119:-

"Although the majority decision of the Board in the recent Judgment in the 20% Case and on the review of the 21% Case, would seem to have resulted in a decision in favour of the straight line method, a reading of the Judgment suggests that this view was adopted by the majority judgment for the purpose only of revising the Judgment in the 21% C se. The subsequent reference in the majority Judgment to the provisions of Paragraph 2(d) of Order-in-Council O.C. 6033 suggests that in the Board's view, final determination of this question may well await the recommendations of your Commission. This view would seem to mean that consideration of the method of depreciation to be adopted for uniformity of accounts, is a matter for your Commission to determine under Order-in-Council P.C. 6033. That is to say, the view appears to be that it is for your Commission to recommend whether, for example, the user method or the straight line method should be adopted. It is submitted, however, that this view does not require your Commission to give consideration to the rates which which should be applied under either method of depreciation. In the light of the above view, the following further submissions are now put to you.

In the 20% Freight Rates Case, counsel for the Canadian Pacific analyzed the evidence in respect of respect of the 'user" basis as presented not only in the 20% Case but in the preceding 21% Case as well (see Volume 816, pages 4038-61).

Accounting experts called as witnesses by Canadian Pacific in the two rate cases gave strong support to the Company's depreciation policies and practices. Mr. George O. May, acknowledged dean of the accounting profession in the United States today and former senior partner of the American firm of Price, Waterhouse & Company, gave evidence that in his opinion the user method 'is theoretically preferable and practically wiser' (Transcript 21% Case, page 15499); that he regarded it as 'an advance on previous practice' (page 15505); and described the user method as a 'superior method' (page 15524).

Mr. J. Grant Glassco, already mentioned as having recorded in the 21% Case the definition of depreciation adopted by the American Institute of Accountants, gave evidence in that case that the user basis is an 'ideal method' (page 15304).

Mr. J.C. Thompson, senior partner in Canada of Peat, Marwick, Mitchell & Company, and widely recognized in Canada as an expert in accounting matters, in his evidence said that 'the user basis is particularly applicable to a railway' (21% Case, page 14345); and 'The user basis more correctly reflects current wastage' (21% Case, pages 14346 & 14349).

Mr. K. W. Dalglish, senior partner of the firm of Deloitte, Plender, Haskins & Sells, one-time president of the Dominion Association

of Chartered Accountants, former member of the Board of Referees under the Excess Profits Tax Act, gave evidence in the 20% Case that 'in my view, the user basis of depreciation is eminently suitable for railroad accounting because railroads experience violent fluctuations in operations' (page 359) and 'It seems to me that the user basis....is to the advantage of the users of the railroads as they are only called upon to pay amounts for depreciation relative to the service given them' (page 361).

Mr. Paul Grady, partner in the American firm of Price, Waterhouse & Company, experienced utility accountant and chairman in 1939 and 1940 of the Special Committee on Public Utility Accounting of the American Institute of Accountants, appearing in the 20% Case said that he believed the user method provided ' a more equitable charge against periodic income' (page 2708).

Mr. Lionel Kent, Chartered Accountant, who gave evidence for British Columbia, in cross-examination agreed with Mr. May's statement that the user method 'is theoretically preferable and practically wiser' (20% Case, page 3286). He also agreed with Mr. Thompson's statement that 'the user basis more correctly reflects annual wastage' (page 3284).

MR. BRAZIER: Mr. Chairman, at that point I must take exception to reading that into the record, because Mr. Kent has already appeared before this Commission

and given evidence that he did not make that statement, that statement which is attributed to him at the top of page 121.

MR. EVANS: Do you say I misquoted the Transcript?

MR. BRAZIER: You have left part of it out, and it has given a different meaning to what he actually said. He said "...in a particular year it might".

MR. EVANS: Well, I would be glad to put that on the record if you wish.

MR. BRAZIER: This has come up several times previously, Mr. Evans.

THE CHAIRMAN: Well, I think you had better look into that point, and if any changes or striking out are required, we will take it up when we come back.

...RECESS

...UPON RESUMING

MR. EVANS: At the adjournment, Mr. Brazier and I were having a discussion about whether Mr. Kent had been done justice by this reference to his evidence, and all I can say, is that I have not the Transcript here. We tried to do justice to him, and I am content to have Mr. Kent's evidence judged on the exact form in which it appears in the Transcript. That, I think, will satisfy my friend Mr. Brazier.

MR. BRAZIER: I am objecting to putting the words "the user basis more correctly reflects annual wastage" as a direct quotation from Mr. Kent's evidence.

THE CHAIRMAN: You have the statement, have you?

MR. BRAZIER: We read it the other day, and it is on page 14960 of the Transcript of this Commission, Volume 73.

THE CHAIRMAN: That is only a quotation of the Transcript. I think we ought to get the Transcript.

MR. BRAZIER: We had the Transcript itself here that day, and the quotation actually reads:-

"It might more correctly reflect current wastage in one particular year, yes, Mr. Evans."

Those are the words that Mr. Kent actually used.

THE CHAIRMAN: Yes, we have the correction now.

MR. EVANS: Well, I want to look at the Transcript, because I do not think that is the only answer he gave.

THE CHAIRMAN: No, but as far as Mr. Brazier goes, we have it.

MR. EVANS: I am quite content to have it judged on the exact language he used in the Transcript.

THE CHAIRMAN: All right, we can go back to that later.

MR. EVANS: "Mr. Kent also agreed (page 3885) that the user method is flexible, although he would not agree that the straight line method is rigid. Mr. Walter MacDonald, for the Province of Manitoba, had agreed in the 21% Case (page 12624) that the straight line method is rigid; the user basis flexible.

Canadian Pacific submits that the evidence in the two rate cases strongly supports the 'user' basis and that no effective attack was made upon it.

In application of the 'user' method of allocating depreciation, railways have a distinct natural advantage over most utilities in that they have fairly homogeneous statistical units -

in gross ton miles, locomotive miles and car miles - with which to measure production.

Canadian Pacific submits that the 'user' depreciation method has substantial advantages not only to the railway company but also to the users of railway service and to the railway's employees. To the man who 'pays the freight' the 'user' basis ensures that the element of depreciation cost remains proportionately the same regardless of the business cycle. To the railway workers it tends towards stabilization of employment, as opposed, for instance, to the 'straight-line' method which requires the same dollar charge in a year of low business volume as in a year of high business volume and thus inclines to curtail the amount of maintenance work which might otherwise be done during depressed traffic years when prices are relatively low. It is difficult to restore a work deficiency of this nature in a period of high business volume because of the shortages in materials and the price rises which usually accompany such a period.

In the opinion of the Canadian Pacific, any statutory direction prescribing a uniform system of accounts should be exceedingly general in character in order to avoid hampering and inhibiting the Board in the exercise of its administrative functions. Over the years there has been a constantly expanding development of information and the way ought to be left open to

the railways to avail themselves currently of such developments, under the supervision of the Board."

THE CHAIRMAN: I think there was agreement on this, that we should not recommend any statutory changes to the Board on this question of depreciation. I think the other day that is what we heard from counsel for the provinces. Is that right, Mr. Frawley, do you remember?

MR. FRAWLEY: I think that is right, sir, yes, as far as I am concerned.

MR. SHEPARD: Perhaps I should say a word. I think that Manitoba may be suggesting an amendment with reference to depreciation, but only that the Board be required to fix the method of depreciation, and that the Board be required to fix the rate.

MR. McLEAN: The same in that respect as the American system. The Interstate Commerce Commission prescribe the rates of depreciation.

THE CHAIRMAN: You think then, that the railways ought not to be left free, and that the Board ought to prescribe the method?

MR. McLEAN: Prescribe the method and the rates

THE CHAIRMAN: Mr. Evans thinks the railways ought to be free, I gather.

MR. EVANS: The railways ought to be given an option. If there is anything prescribed, it ought to be the user basis. If there is to be nothing prescribed, the railways ought to have that option of using the user as against the straight line method if it is left to them.

MR. FRAWLEY: Your lordship will understand that we do not agree with that suggestion, of course.

THE CHAIRMAN: Your suggestion is that the Board should adopt one or the other?

MR. FRAWLEY: Yes, as long as it is uniform.

THE CHAIRMAN: Uniform with a rather strong leaning on your part to the straight line method?

COMMISSIONER ANGUS: When you say "the railway" do you mean each railway by itself?

MR. EVANS: Yes, we think that if, for example, the Canadian National prefers the straight line we do not want to force them to take the user method. We think we should have the right to have the user method.

MR. McLEAN: How could you have uniform accounts then?

MR. EVANS: I am answering a question by Commissioner Angus.

COMMISSIONER INNIS: Would there be some difficulty for example, in the policy towards labour? In the Canadian Pacific presumably it would be more advantageous to have the user method. Now, if that were not the case on the Canadian National, there would be two separate labour policies?

MR. EVANS: I do not know that there would be two separate labour policies, but I think the point we make about labour, is this, that in a period of depression, if a straight line method is used, a larger proportion of revenue is used up in setting aside depreciation which pays no attention to fluctuations in volume of work done.

Now, if you are going to avoid an operating deficit, you will have less money to spend on maintenance work in those periods. Now that, as we say in our Brief, is the time when costs are low and you should be doing it. Now we say, that with a user method it fluctuates with traffic

volume to some extent and that you will, in periods of depression, have some money left out of a given amount of revenue to spend on maintenance when it can be done cheaply.

COMMISSIONER INNIS: Yes, but if you allow the Canadian National to follow the other policy, then you have discordance between one point of the country and the other depending on which railway they are served by.

MR. EVANS: We would submit no, sir, for this reason. There might be several ways you would want to use comparisons. Quite obviously comparisons of operating results and efficiency could be made by eliminating depreciation. Now, if you want to compare results, you will always rationalize depreciation accruals to the straight line method; in other words, you will go into the depreciation charges and you can rationalize those charges in terms of service life in years, if you want to do so. We did that on a great number of exhibits in both the Rate Cases. If you take a period of high and low traffic volume and average your accruals and express them as a percentage of your investment, you will come out with a figure which represents the straight line rate and you can quite easily rationalize that.

COMMISSIONER ANGUS: But the fluctuations in net incomes of the two railways would not be strictly comparable?

MR. EVANS: That is probably true, but we think they never are anyway. For instance, we pay income tax and the other principal line does not pay income tax. There are quite different results when you get past operating expenses.

COMMISSIONER ANGUS: But if any changes were made in the direction of greater comparability, this would be because the scheme had changed.

MR. EVANS: There would be no doubt that this would be something short of complete and absolute uniformity, but that is our submission and we feel that uniformity is desirable and we say if absolute uniformity must be achieved, then we think it ought to be the user method, because we say with the experts we called that we made a very strong case for the user method. We think that the case we made there is deserving of every consideration, and if it becomes a matter in issue here, then we propose to say to this Commission: "Weigh the evidence which the Board had before it," and that is all we ask them to do, - "weigh it" and if they do not come to the conclusion that the weight of evidence is not in favour of the user method, I must say I will be quite surprised, because the weight of evidence was there, and there was not, as I submit, any real attack made on the user method.

(Page 16705 follows)

MR FRAWLEY: Does my friend mean, when he just last spoke, that the Board should weigh the evidence which he recites, merely catalogues and recites, on page 120 -- that this Commission should review the evidence of Mr. Grant Glassco, Mr. Thompson, Mr. Dalglish and Mr. Grady from New York?

THE CHAIRMAN: Well, I think Mr. Evans referred to the Board.

MR EVANS: No, sir; what I said was this: I said if it becomes important to this Commission to consider that question as part of the matter of uniformity of accounts---

THE CHAIRMAN: We have to go into the question of depreciation; we are instructed to.

MR EVANS: Yes. Now, I say if it becomes important that you consider method, then I say to the Commission, you should weigh the evidence that was presented to the Board, because we do not want to go through all that again. All those witnesses were cross-examined, they have expressed their opinions, and, as we say in our brief, we hope that the Commission would look at that evidence and consider and weigh it and form their independent conclusion about it. The strength of it is such that I am content to have this Commission weigh that evidence, read it and decide for themselves whether we made a case or did not, on that evidence.

COMMISSIONER ANGUS: I gather that you are somewhat opposed to saying that it should be the same for both, that the rule should be the same for both railways, and therefore be fixed by the Board of Transport Commissioners.

MR EVANS: Well, perhaps there are two parts to that question. I think the Board unquestionably should decide the method. I think when it comes down to uniformity

that if there must be absolute uniformity it should be the user method, but I concede this, that I do not think that the slavish -- if I may put it that way -- the slavish desire for uniformity should necessarily force one of the railways that does not want to adopt that to adopt it, because I do not think it is so necessary that there be absolute uniformity that you need go that far.

THE CHAIRMAN: Well, apparently you would proceed cautiously, in two steps. In the first place you say that any statutory direction prescribing a uniform system of accounts should be exceedingly general in character.

MR EVANS: Yes, sir.

THE CHAIRMAN: In order to avoid hampering and inhibiting the Board in the exercise of its administrative functions. Now, there is one thing.

MR EVANS: Yes, sir.

THE CHAIRMAN: Being careful about the Board. Then, secondly, you say that over the years there has been a constantly expanding development of information and the way ought to be left open to the railways to avail themselves currently of such developments, under the supervision of the Board. So that the uniform system would be thinned out in two directions; first, it would leave a very wide latitude to the Board, and then the Board in turn leave a wide latitude to the railways.

MR EVANS: Well, not too wide a latitude to the railways; only to let them---

THE CHAIRMAN: Well, the way ought to be left open to the railways to avail themselves currently of such developments -- of course, you say, under the supervision of the Board, that is true.

MR EVANS: Yes.

THE CHAIRMAN: Well, that is your attitude.

MR EVANS: Yes, sir.

THE CHAIRMAN: Now, before we pass on, I would like to make sure, on that paragraph I have just read, whether or not there is any difference between the position taken by Alberta and that taken by Manitoba. I rather gather that there is some difference. Will you clear that up, Mr. Frawley?

MR FRAWLEY: Just, my lord, that we have nothing to recommend by way of an amendment. I understand Mr. McLean proposes to offer some amendment.

THE CHAIRMAN: Do you propose, Mr. McLean, to submit an amendment on this?

MR MCLEAN: Yes, my lord.

THE CHAIRMAN: Then when we have your amendment we will discuss it.

MR EVANS: I have almost finished the portion I wanted to read, but perhaps I may just finish that page, reading again from page 122 of Part I of the brief:

> "In concluding this part of its submission, it is essential that attention should be directed to a problem, while not necessarily related to depreciation accruals, nevertheless results from the application of orthodox accounting as presently practised. Orthodox accounting requires that original cost form the base of depreciation and in periods of stable prices the accruals on this basis would naturally provide for the replacement of assets. The drastic elevation of price levels, however, means that depreciation accruals based on original cost fall far short of meeting replacement requirements. Canadian Pacific, for example, is currently charging depreciation based on the original cost of locomotives purchased for $20,000 or $30,000 which cannot be replaced for much less than $150,000

at today's prices. Large increases have also taken place in the prices of other items of the Company's assets which now and in the future require to be replaced.

The financial aspect of this situation far overshadows the importance of any differences in opinion among accountants in regard to questions affecting depreciation calculations. While there is diversity of opinion as to the policies and practices which should be adopted to cope with rising investment costs, there is general agreement by businessmen, economists, accountants and others as to its effect. The dominant considerations of the future must inevitably lie in the direction of ways and means of securing adequate funds for replacement of facilities. The situation is far more serious for public utilities than for most other businesses because utilities have relatively large investment in plant in proportion to income and because of the low rate of capital turnover inherent in their operations."

COMMISSIONER ANGUS: Mr. Evans, does the middle paragraph there bring in two considerations ? You speak of the drastic elevation of price levels; in the example of the locomotives, is the locomotive that costs $150,000 a locomotive with the same power as the one that costs $20,000, or is it a different type of locomotive?

MR EVANS: It very probably is a more modern locomotive, but what we are trying to say there is that a locomotive -- without being too exact about it -- which cost $20,000 or $30,000 when it was originally built, if you were to replace that locomotive you would probably have to pay $150,000 for it. We have big modern locomotives that cost up to $300,000. I am not trying to tie myself

down to a particular locomotive, but merely to illustrate that when you are doing it on a cost basis, today you are depreciating the locomotive you bought twenty or twenty-five years ago, and you may be depreciating a locomotive which to replace today would cost four to five times what the original cost was.

COMMISSIONER ANGUS: It is a replacement less a betterment, really, isn't it?

MR EVANS: It may be. If there is an element of betterment, then of course it is new capital under renewal accounting.

COMMISSIONER INNIS: Was the omission of deflation deliberate ? That is, you have the reverse---

MR EVANS: No, sir. We think the trend of events pretty substantially, with minor recessions, has been upwards in prices, and we think that that may well be a more or less permanent thing, though perhaps not so abrupt or quick as it has been in recent years.

COMMISSIONER INNIS: What would your policy have been during the period of depression, when the prices had fallen? Would you be in a position then to say, "We have built these locomotives and so on during a period of high prices, and we have come down to a period of low prices"?

MR EVANS: I think my position must have been this, that if it could be shown that our depreciation accruals on cost were more than they needed to be, the Board would quite likely look at the rate and say that we should reduce the rate. But the brief does not advocate that this is a problem that has to be taken care of in depreciation; it simply points up a problem which we think is closely related to depreciation. No solution has been found -- there is still a difference of opinion about it -- but we only point it up as something that is necessary to an under-

standing of the problem. We do not ask to have our rate fixed on a replacement basis, although that is essentially what you do when you go in for renewal accounting instead of depreciation accounting.

Q. Now, Mr. Liddy, we have been talking in this portion I have read about fluctuations in traffic. Have you a statement which shows the fluctuations in traffic over a period of years of the Canadian Pacific?

A. Yes, I have a statement, Mr. Evans.

MR EVANS: That is Exhibit 188.

---EXHIBIT 188: C.P.R. selected transportation and traffic statistics, 1924 to 1948.

MR EVANS: Q. That statement shows what, Mr.Liddy?

A. This statement shows the fluctuation in selected transportation and traffic statistics over---

THE CHAIRMAN: Pardon me. Are you talking of Exhibit 188?

MR EVANS: Exhibit 188, yes, sir.

MR O'DONNELL: Better read the heading.

MR EVANS: My friend suggests I read the heading. It is entitled "Canadian Pacific Railway Company - Selected Transportation and Traffic Statistics - Years 1924-1948." It consists of a date column and six other columns.

Q. That exhibit, Mr. Liddy, shows by years the revenue freight ton miles, revenue passenger miles, gross ton miles in transportation service, locomotive miles in transportation service, freight car miles in transportation service, and passenger car miles in transportation service. Now, would you be good enough to point out to the Commission the extent of the fluctuations in traffic which that exhibit shows the Canadian Pacific to have experienced over the past twenty-five years?

A. Yes. For that purpose, Mr. Evans, I have divided Exhibit 188 into three periods -- the pre-depression period---

Q. When you say divided, I gather you mean by that the underlining after the year 1928 right across those various columns?

A. Yes. That underlining in 1938 is the maximum figures that those statistics in each of those columns reached in that pre-depression period.

Q. I see.

A. In the depression . period I have also underlined the minimum statistics reached during that period.

Q. Yes?

A. And in the war and post-war -- recent war and post-war period, I have underlined the maximum statistics reached in that period.

Q. Now, take the period from 1928 to 1933; could you give the Commission the extent of the fluctuations percentagewise?

A. Yes. Take the first column---

Q. Revenue freight ton miles?

A. Dealing with revenue freight ton miles. These were in 1928 18,059 millions. They declined in 1933 to 9,353 millions.

Q. That was a percentage---

A. Decline of 48 per cent. Now, dealing with the next column, the revenue passenger miles, the decline from 1928 to 1933 was 54 per cent.

Q. Then the next column?

A. The decline in gross ton miles was 43 per cent; in locomotive miles it was 37 per cent; in freight car miles it was 45 per cent; and in passenger car miles it was 33 per cent.

THE CHAIRMAN: Would you please give me the first two columns again in percentages? I did not get them down.

MR EVANS: He gave 48 per cent for revenue freight ton miles, and 54 per cent for revenue passenger miles. That is from 1928 to 1933.

Q. Now, taking the period from 1928 to 1944, would you give some figures to indicate fluctuations?

A. In 1928 the revenue freight ton miles were 18,059 millions; in 1944 they were 27,375 millions. That is an increase from 1928 to 1944 of 52 per cent.

Q. That is to say, from your pre-depression high to 1944 you had an increase in revenue freight ton miles of 52 per cent. Now, what is the corresponding percentage for the next column, revenue passenger miles?

A. The increase was 123 per cent.

Q. And in gross ton miles?

A. 35 per cent.

Q. And locomotive miles?

A. 16 per cent.

Q. In freight car miles in transportation service?

A. 18 per cent.

Q. And passenger car miles in transportation service?

A. 21 per cent.

Q. Now, will you take the period from the low point of the depression to 1944 and see what happened percentagewise?

A. Yes. Revenue freight ton miles in 1933 were 9,353 millions, and in 1944 were 27,375 millions. That is an increase of 193 per cent.

Q. And in the next column, revenue passenger miles, the corresponding increase was what?

THE CHAIRMAN: What did you say? 193 per cent?

MR EVANS: 193 per cent.

THE WITNESS: Increase, yes, sir. And revenue passenger miles, the increase was 383 per cent.

MR EVANS: Q. And in gross ton miles?

A. 139 per cent.

Q. And locomotive miles?

A. 81 per cent.

Q. And freight car miles?

A. 117 per cent.

Q. And in the final column, passenger car miles?

A. 80 per cent.

Q. Now, having regard to what you have said about the user method of depreciation and these fluctuations that have taken place over the years in the statistics, can you give the Commission a simple illustration of the practical result of the application of the user method as compared with the straight line method, so as to take into account these fluctuations in traffic that are shown by that exhibit?

A. If, Mr. Evans, one were to find three years in which the traffic volume in the first year was 30 per cent below average, and in the second year average, and in the third year 30 per cent above average, and the accruals under the straight line basis of depreciation were $20 million a year, then the user method in the first year -- that is, the year below average -- would be $14 million, and in the average year, the same as the straight line rate, $20 million, and in the year 30 per cent above average it would be $26 million.

Q. That all assumes that your service lives are the same under both methods?

A. That is right. Thus, taking the three-year period together, the user rates aggregate $60 million of depreciation, the same as three years of straight line

rates of $20 million.

Q. In saying that are you saying that as long as your rates are the same, and having regard to service lives, the accruals over a period of years in which you will have the ups and downs of traffic, under the user method, will be the same as under the straight line method?

A. Yes, that is the situation, Mr. Evans.

THE CHAIRMAN: Well, it is time to adjourn now, Mr. Evans, and I wish to say that, pursuant to a suggestion made to us, we will meet tomorrow at 10:45 instead of 10:30.

---The Commission adjourned at 4:45 p.m., to meet again at 10:45 a.m. on Wednesday, March 1, 1950.

A.R

ROYAL COMMISSION ON TRANSPORTATION

EVIDENCE HEARD ON

MAR 1 1950

VOLUME

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ROYAL COMMISSION ON TRANSPORTATION

OTTAWA, ONTARIO,
WEDNESDAY,
March 1, 1950.

THE HONOURABLE W.F.A. TURGEON, K.C., LL.D.	-	CHAIRMAN
HAROLD ADAMS INNIS	-	COMMISSIONER
HENRY FORBES ANGUS	-	COMMISSIONER

G.R. Hunter
Secretary

P.L. Belcourt
Asst. Secretary

COUNSEL APPEARING:

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H.E. O'Donnell, K.C. H.C. Friel, K.C.	Canadian National Railways
F.C.S. Evans, K.C. I.D. Sinclair	Canadian Pacific Railway
C.D. Shepard Wilson McLean, K.C.	Province of Manitoba
M.A. MacPherson	Province of Saskatchewan
J.J. Frawley, K.C.	Province of Alberta
F.D. Smith, K.C.	Province of Nova Scotia; Transportation Commission of the Maritime Board of Trade
J. Paul Barry	Province of New Brunswick
C.W. Brazier	Province of British Columbia

Ottawa, Ontario,
Wednesday, March 1, 1950

MORNING SESSION

---The Commission resumed at 10.45 a.m.

THE CHAIRMAN: All right, Mr. Evans.

MR. EVANS: Before I go ahead with Mr. Liddy, my lord, I would like to speak to a matter that came up yesterday.

THE CHAIRMAN: Very well.

MR. EVANS: I should like to refer to the transcript at page 16661, where there was some exchange between Mr. Smith and myself. I refer to the bottom of page 16661:

"Mr. Evans: I would say no --"

We were there discussing this question of appreciated investment basis.

"I would say no, because you made the suggestion --"

I was speaking to Mr. MacPherson.

"-- that you could not have a rate base without an estimate of value or at least Mr. Smith did.

"Mr. Smith: That is not correct - unequivocally not correct."

I am sure Mr. Smith would perhaps be happy to have his attention directed to a discussion on the 20 per cent case at page 1409. I am now reading from Mr. Smith's argument.

MR. MacPHERSON: My lord, might it not be better to leave this matter until Mr. Smith is here?

MR. EVANS: I thought he would be here.

MR. MacPHERSON: Mr. Smith is not here.

MR. EVANS: Then I shall certainly leave it.

S. J. W. LIDDY, RECALLED

EXAMINATION BY MR. EVANS (Cont'd)

Q. Now, Mr. Liddy, before we proceed, in yesterday's transcript I asked you this question:

> "Mr. Liddy, are results which were obtained on page 116 of the Appendix to Part I on a comparable basis with those shown on Exhibit 180?"

Your answer was:

> "Well, it is true, as Mr. Brazier says, that there are small amounts of incidental revenue. I think they amount to about $7,000, but not enough to affect the basis, Mr. Brazier."

At that stage of the transcript we were discussing the comparability of dividing the revenues and expenses as between freight and passengers. That is, Exhibit 180. Mr. Brazier suggested they were not comparable, and your answer was, except for these incidental revenues that was not so. I understand you have something more you would like to say on that?

A. Yes, Mr. Evans. The statement appearing at page 116 of the Appendix to Part I, in addition to showing the railway operating expense also shows an item for taxation, hired equipment and joint facility rents. There is no corresponding item to this on Exhibit 180; therefore, in comparing the systems net income deficit shown on Exhibit 180 with that given in the Appendix, the figure should be taken before you arrive at taxation.

Q. So that if that were done the figure of the western passenger deficit, if that were taken out it would be something like $17,868,000?

A. Yes, sir.

Q. Instead of $18,555,000?

A. That is right.

[illegible]

[illegible] 7, 00, but [illegible]

[illegible] the [illegible] was discussing the [illegible]

Mr. [illegible] suggest[illegible] were not comparable, [illegible]

was not so. I understand you h[illegible] something more. you

[illegible] Yes, [illegible] The [illegible] of operating [illegible]

[illegible] to [illegible] to [illegible]

[illegible]

[illegible] if the [illegible] were taken [illegible]

would [illegible]

Q. That would be the corresponding figure, subject to that few dollars difference you spoke of, with the system's figure given in the exhibit?

A. That is right.

THE CHAIRMAN: Will you give me that figure you just gave from Exhibit 180, from which this subtraction must be made?

MR. EVANS: It is not shown on the exhibit. You subtract the revenue figure from the expense figure; the resulting figure was put on the record, and was $28,866,961; and in the evidence yesterday we suggested the deduction of the western figures shown on page 116 of Part I of the brief, of $18,555,000 odd, leaving a deficit of $10,000,000 odd. Mr. Liddy says in order to make the correct comparability the deduction, instead of being $18,555,000, should be $17,862,000. It makes a difference of some $700,000.

Q. Now, at the close of yesterday, Mr. Liddy, just to bring you back to the point, you had said:

> " . . . having regard to service lives, the accruals over a period of years in which you will have the ups and downs of traffic, under the user method, will be the same as under the straight line method."

Assuming, the same service lives apply to both methods. Would it be fair, in summarizing what you said yesterday afternoon, to say that it comes down to a choice of the most suitable method of depreciation for allocation and depreciation, as between the various years?

A. Yes, Mr. Evans. It is as simple as that. Any method of depreciation that does not recognize the considerable fluctuations that exist in railway traffic, must inevitably have a serious drawback. A rigid method

of allocation of depreciation as between the years means that in good times less depreciation will be allocated. per unit of traffic, than would be the case under average traffic conditions. Conversely, in poor times more depreciation will be allocated per unit of traffic.

In my view the ideal method is to so allocate the depreciation provisions as between years to effect as even a burden per unit of traffic as is possible, and consistent with sound accounting practices.

Q. Now, you may recall that when I was reading to the Commission some pages from the brief on this question, I read these words on page 121:

> "Canadian Pacific submits that the user depreciation method has substantial advantages."

I wonder if you would care to elaborate a little on that? Would you divide it up? Would you first give the advantages to the railway company and then the advantages to the users, and so on?

A. First, Mr. Evans, as to the advantage to the railways company, these are:(1) the accounts being realistically stated as between months and as between years more nearly in relation to the volume of business being done, is an aid to managerial direction and control. (2) The flexibility of user depreciation method places the provision for depreciation on a parity with other items of expense which go up and down with the traffic moving. (3) In periods of hard times it is not always desirable, or even possible, to recover from users the same gross amount of depreciation as in good years.

Q. Then as to the management standpoint, how would you summarize that?

A. From the management point of view the user depreciation method is desirable, and in my opinion it is

an advance over other methods.

Q. Now having dealt with the management standpoint, what about the advantage, if any, to the users of the service?

A. First I would like to say that the advantages which exist for the railway will react to the advantage of the users.

Q Now when you say that you, I suppose, identify the long run interests of the user and the railway, to some extent?

A. Yes, I believe their interests are inseparable.

COMMISSIONER INNIS: Q. What is the significance of the user method as far as the railway is concerned as regards income tax? Does it involve a different calculation from that of the sraight line?

A. Yes, Dr. Innis, it involves a different calculation. The income tax people, sir, have usually been content to fix maximums and allow companies to charge out in the way of depreciation anything they wish under that ceiling. In poor times they may arbitrarily say it would be 50 per cent. You can see, Dr. Innis, that with a regulated company attempting a method of that kind, one year half and another year double, that there would be difficulty say in rate cases. I feel you have got to have a systematic and rational plan if you are regulating an industry.

MR. EVANS: Q. Just to clear that up perhaps one further step, is my understanding correct that the income tax is based on what is known as the diminishing balance basis?

A. It is, Mr. Evans, commencing with the year 1950.

COMMISSIONER INNIS: Q. What do you mean by

"diminishing balance"?

MR. EVANS: Perhaps, Mr. Liddy, you can answer Dr. Innis as to what is meant by diminishing balance?

A. Once having taken depreciation for income tax purposes, you cannot again recover that depreciation.

Q. It comes off the investment; in other words, it is depreciable investment, reduced by whatever you take off?

A. That is right.

Q. Am I right that you recalculate your depreciation in the next year for income tax purposes having regard to the then depreciation basis?

A. Yes, it goes on year by year that way.

(Page 16721 follows)

N

MR. EVANS: Does that perhaps help you?

COMMISSIONER INNIS: Yes.

MR. EVANS: Now then, you were saying that you thought that the interests of the user and the railway were inseparable? Have you anything to say about the equitability of the user basis in periods of high traffic volume?

A. When the business level is good and railway traffic is moving in volume, I consider it is only equitable that individual railway users should contribute equally as much per unit on traffic as would individual railway users contribute during periods of depression per unit of traffic.

Q. Now, we have a third category which is mentioned in the brief. In what way do you suggest that the user method has an advantage over other methods having regard to railway employment?

A. I believe the flexibility of the user basis tends to stabilize railway employment. In poor times, railway management is hard pressed to make economies in the use of labour and material. To the extent that depreciation charges are lighter during low traffic years, there will be less pressure on management to reduce expenses by curtailing employment. It is a distinct economic advantage as the need for employment is highest during subnormal periods and it is during such periods that the greatest volume of maintenance work can be done at the lowest cost.

Q. Would you relate that same advantage to the user in some way, the user of railway services?

A. Yes, this advantage will also inure to the benefit of the railway user. In fact, all the advantages of user depreciation must inevitably inure to the benefit of the

railway user, whether or not they may be classified in the first instance as advantages to the railway management or railway labour.

Q. Now, have you anything to add on that subject?

A. Nothing, Mr. Evans, except to summarize my views and belief that the advantages of the user method are many and compelling, that the user method is much superior, more practical, and an advance over the straight line method and that any uniform classification prescribed for Canadian railways should provide at least an option for any railway company to adopt that method if it chooses to do so.

THE CHAIRMAN: Now, Mr. Evans, how far do you want us to go in this question? Are you in the same position as Mr. Frawley, only he, of course, is on another question, but do you say that you wish us to recommend legislation about this or not?

MR. EVANS: No, sir, not specifically, but I say this: if you do recommend legislation with regard to uniform accounting, and it involves any reference to depreciation methods, we ask that you recommend the user method if it must be completely uniform. If there is to be something short of complete uniformity, then we think there ought to be an option by either railway to adopt that method which it feels is desirable.

THE CHAIRMAN: Yes, I see; you want to have freedom?

MR. EVANS: We want to have freedom and if we cannot have freedom, we think the recommendation should be that the user method be adopted.

THE CHAIRMAN: You think freedom can be accorded without breaking into the principle of uniform accounting?

MR. EVANS: Well, as I said yesterday, it does result in something less than absolute uniformity, but, as I said yesterday, I think that absolute uniformity may be too rigid a goal to seek, because after all there are small differences in even uniform accounting systems as between railways and the way they keep their accounts and the way they interpret rules and so on that must make for greater differences than would be expected. So that I would submit that absolute uniformity is perhaps unattainable. When you want to get a complete comparison of results between two large railway systems such as the two in this country, the differences are too fundamental between them in a great many ways to make absolute comparisons. What you can get are absolute operating comparisons, and that is efficiency figures and the like which enable you to see whether one or the other is being operated efficiently, but whether absolute uniformity can be achieved or should be achieved, that is another matter. We think it can only be achieved by a very, very careful examination of all these problems worked out with the Board and the railways.

THE CHAIRMAN: All right.

MR. EVANS: Now then, turning to pages 125 to 128 -

THE CHAIRMAN: Of Part I?

MR. EVANS: Of Part I, sir, the paragraph of the outline submission, Item 65, which says:-

> "65. With regard to the segregation of assets between rail and non-rail operations, Canadian Pacific keeps its accounts in such a way as to enable an adequate segregation to be made except in the case of working capital, which must always be a matter of judgment. No

legislation is required to enable a complete segregation to be made and Canadian Pacific supplied such material recently to the Board of Transport Commissioners".

And then, at page 127, at the bottom of the page, this appears:

"In summary, the Canadian Pacific investment in railway property is clearly segregated from non-railway investment on the Balance Sheet, and there is supplied to the Board and the Bureau of Statistics the figure of 'Investment in Property Used in Transportation Service' which is the relevant base for testing railway results".

Now then, do I gather that it is your view from those statements that investments in non-railway properties should not be included in the investment base for railway transportation results?

A. That is right. In reply to one of your earlier questions, I think I pointed out that one of the first principles to be followed in designing a Canadian railway classification is that it should be confined to showing the result of transporting goods and passengers on the facilities of the carriers which are required for the purpose of providing railway transportation service. It is, therefore, my view that this principle must, as a matter of course, apply to the railway investment account as well as the railway income account.

Q. Well now, what do you say would be proper in order to have a firm base for testing the adequacy or otherwise of railway results?

A. It seems to me that when the average level of

railway rates comes into the question as being either too high or too low, the problem is reduced to its simplest terms if we have in readily available form on the one hand the income result which is derived solely from railway transportation service, and, on the other hand, the amount of the investment in facilities which are used to provide that service.

Q. Would there be complications, if the non-transportation income and investment were included in the railway account?

A. Yes, that would be obvious. I believe that such a procedure would impede the progress of rate cases and after all, whether non-transportation endeavours are profitable or not should have no bearing on the fixing of railway rates.

Q. In the majority judgment of the Board of Transport Commissioners dated September 20, 1949, reference was made on page 13 to 8 enterprises which provincial counsel suggested should be included in railway income, because they are directly connected with the railway service. Have you a statement showing the 1947 results - I think the 1948 results, isn't it?

A. No, theyear 1947.

Q. The 1947 results of these enterprises?

A. Yes, I have a statement for the purpose of filing, Mr. Evans.

Q. And does that statement show also the investment of the Company in those enterprises?

A. Yes.

Q. And that will be Exhibit 189. It is entitled "Earnings and Investment in Enterprises which have been

Suggested from Time to Time as Being Includable in Canadian Pacific's 'Railway' Account as Listed in Judgment of Board of Transport Commissioners dated September 20, 1949".

...EXHIBIT 189:-	..filed by Mr. Evans	: Earnings and Investment in Enterprises Which Have Been Suggested From Time to Time as Being Includable in Canadian Pacific's "Railway" Account as Listed in Judgment of B.T.C. Dated September 20, 1949.

Q. Cont. Now, before I ask you to discuss that Exhibit, I think there is an addition on the bottom of that which is not included in the Board's list. Is that "hotels" Item 9?

A. Yes, I show on this Exhibit 189 the results of hotels which was not one of the items listed on page 13 of the Board's Judgment. I did that because in these proceedings, Mr. Evans, some suggestions were made that hotels should be taken into the railway operations.

Q. Then, would you tell the Commission what that Exhibit shows?

A. This Exhibit 189 shows, that for the year 1947 the nine enterprises listed produced net income of $4,471,176 and that the investment in those enterprises was $118,360,554.

Q. And the rate of return on that investment provided by the income from them?

A. That works out to a ratio of income to investment of 3.78%.

Q. That is the last figure on the Exhibit?

A. Yes.

MR. FRAWLEY: Has Mr. Liddy figured it out individually, each of the nine items?

MR. EVANS: No, but I am sure my friend can just do

that right across the page. Have you made the individual calculations on rate of return?

A. No, some are above the average and some are below the average.

COMMISSIONER INNIS: What is the significance of this difference between cost of investment or par value of the principal amount of stocks and bonds?

A. Take our communications, for example, Dr. Innis, that would be the cost of the investment.

MR. EVANS: You mean the cost of the properties providing the service?

A. Yes.

Q. There are no stocks and bonds in the communications department?

A. No, but the $3 million for the Canadian Pacific Express Company is the capital stock.

COMMISSIONER INNIS: Par value?

A. That is right, and so on.

MR. FRAWLEY: Perhaps if you went down the lines it would only take a minute, and indicate which is which in each case?

MR. EVANS: Go ahead, Mr. Liddy. That represents the Canadian Pacific holding of Canadian Pacific Express Company stock - that $3 million. Now, the Fredericton and Grand Lake Coal and Railway Company - what does that item of $605,000 represent?

A. Well, from memory, Mr. Evans, it represents capital stock and bonds.

MR. FRAWLEY: Mr. Evans, I really should not have bothered; it appears on page 13 of the Judgment, stocks and bonds, and I think with the exception of the Express and

the Communications, it is all here.

MR. EVANS: Well, hotels probably - that represents the actual investment in the property in hotels?

A. Yes, the net investment after depreciation.

THE CHAIRMAN: Are we talking about the Fredericton and Grand Lake Coal and Railway Company?

MR. EVANS: Well, the witness said that according to his memory that was stocks and bonds of that Company, and Mr. Frawley interjected to say, that in the Board's Judgment it is really shown that some of each are held, and I simply drew attention then to the item of "hotels" as the only item in which it was not a question of stocks and bonds but which represented an actual investment in physical property.

COMMISSIONER ANGUS: Were these eight items discussed individually, or proposed individually, or was it more or less agreed that all should be in or all out?

MR. EVANS: No, there was no agreement on any of them. There was a substantial amount of argument both in the 20 Per cent and 21 Per cent Cases about the necessity or otherwise of having them in.

COMMISSIONER ANGUS: I meant, was the argument that all should be in or all out, or was there a special argument on each one?

MR. EVANS: There was a special argument on each one.

THE CHAIRMAN: You would argue them all out?

MR. EVANS: Yes, sir, for different reasons in many cases, but all in principle for the same reason.

Now then, you have given us, Mr. Liddy, the figure of return on Exhibit 189 derived from these enterprises.

Now, apart from the question of earnings on the properties, what is your view as to the propriety or otherwise of including them in railway earnins?

A. On looking over the list, Mr. Evans, I can see no justification for mingling such earnings and investments with the railway earnings and investments. The results which are shown here for communications, for example - -

Q. That is the first item on the Exhibit?

A. Yes, are related only to the public service of transmitting messages in competition, if you like, with the telephone companies and under the form of public regulation which is in effect for communication companies.

Q. Now, when you speak of "public regulation", that is by the Board of Transport Commissioners under the Railway Act?

A. Yes, sir. Such telegraph and wire services as are required in the operation of the railway are paid for by the railway at cost, and the amounts so paid are duly reflected in railway operating expenses.

Q. Now then, I would like to, before I go on, make a correction in our Brief. I am going to deal next with the Express Company, and I would like to correct a statement made in Part II, page 30. In the middle of the page there is a paragraph beginning: "This is by far the major operation.."

THE CHAIRMAN: Will we strike out that paragraph?

MR. EVANS: No, sir, I am just going to make some technical corrections in language. In paragraph 2 on page 30, it says:-

> "This is by far the major operation of the Express Company. Its subsidiary operations include the sale of money orders and other financial paper. It also has some income from investments. The net income from the sale of commercial

paper, and from investments is the only real net income of the Express Company...".

Now, I ask that this be changed to read as follows. The sentence beginning: "The net income from the sale of commercial paper" should read after the word "paper" -

"...is taken as Other Income of the Canadian Pacific. The income from investments is the only real net income of the Express Company".

and so on. It carries on as it was. It is just a technical change in language.

(Page 16733 follows)

THE CHAIRMAN: You say here, "The net income from the sale of commercial paper"---

MR EVANS: You strike out the word "and" after "paper", sir, and you insert the words "is taken as Other Income of the Canadian Pacific".

THE CHAIRMAN: Do you mean the Canadian Pacific Railway Company?

MR EVANS: Yes, sir.

THE CHAIRMAN: Not the express company.

MR EVANS: No, sir. It is the income of the express Company that is taken into the accounts of the Canadian Pacific as Other Income where it involves the sale of commercial paper. Then you would start the new sentence, "The income from investments and so forth is the only real net income", and so on.

THE CHAIRMAN: I think that was explained yesterday, was it not?

MR EVANS: I do not recall having explained it. It was drawn to my attention as a technical misstatement, and I wanted to correct it.

THE CHAIRMAN: Yes, I think this makes your paragraph conform to the evidence.

MR EVANS: I am reminded that Mr. Liddy did speak to it yesterday. Your memory is quite right, sir.

Q. Now, you have been giving your views as to the lack of justification for including the earnings on investment from communication services; what do you say in this connection with regard to the express business?

A. That is item 2 on Exhibit 189, Mr. Evans?

Q. Yes.

A. The revenues and expenses which pertain to the actual handling of express over the rail facilities are already reflected in the railway income account.

Q. That is outside that item of 286,992 on Exhibit 189?

A. That is right; and the only matter in question here then is that relatively small income.

Q. You say relatively small; you are speaking now of the 286,992 shown on Exhibit 189?

A. Yes.

Q. Now, what have you to say about the return that the Canadian Pacific gets from its investments in the Toronto, Hamilton and Buffalo Railway Company, the Northern Alberta Railways Company and the Toronto Terminals Railway Company? Those are three shown on that same exhibit.

A. Those are items 5, 7 and 8, I think, Mr. Evans.

Q. Yes, 5, 7 and 8.

A. The Canadian Pacific has invested some of its funds in the securities of these companies. These investments are the same in principle as if the company had invested such moneys in say government bonds. These investments are not shown as part of rail investment, and therefore the income from these securities ought not to be treated as rail income. Each of these companies is entitled to earn a reasonable return on the investment in its properties, and to the extent that Canadian Pacific holds securities it naturally receives a proportion of the return which such companies are able to earn. It seems illogical to suggest that the earnings which Canadian P cific receives from them should be added to the return which Canadian Pacific has been able to earn from its railway property.

Q. There is an item on Exhibit 189, the Minneapolis, St.Paul and Sault Ste. Marie Railroad Company; would you express your views with regard to the suggestion to include the earnings from the securities of that company in railway accounts?

[illegible]

[illegible] formed [illegible]

[illegible] company and the [illegible]

[illegible] there [illegible]

[illegible]

[illegible] the statements of these companies. [illegible]

[illegible] principal [illegible] the company [illegible]

[illegible] not shown [illegible] investment, [illegible]

[illegible] from these accounts [illegible] capital [illegible]

[illegible] small income. [illegible]

[illegible] than [illegible]

[illegible]

A. The position with regard to that company is similar to that with regard to the companies which I have just mentioned. In the case of the Soo Line there has been some tendency to point to the fact that the company's guarantee of the interest on certain bonds of the old Soo Line Company places the investments in Soo Line securities in a different category. I should like to explain this situation.

Q. Before you do so, Mr. Liddy, may I put this to you, that the guarantee of bonds is the guarantee on the old Soo Line Company before its recent reorganization?

A. That is right.

Q. And it has now been reorganized, and there is a new company with a slightly different name?

A. Yes.

Q. Now, will you tell us about the guarantee and how it arose?

A. The guarantee of interest on the old Soo Line bonds was given under an agreement made about 1890. This agreement was one by which the Soo Line agreed to give all of its traffic destined to points in Canada to the Canadian Pacific. Thus the consideration for the guarantee was the traffic received under the agreement.

Q. What happens to the earnings from the traffic received under the agreement?

A. Those earnings are included in Canadian Pacific rail earnings.

Q. Now, that being the consideration for the guarantee, what do you say about the payments of interest under the guarantee which have had to be made?

A. I consider the payment of interest under the guarantee should therefore be a charge upon those earnings.

COMMISSIONER INNIS: Have there been years in which you have had to pay?

MR EVANS: Oh, yes. What happened, sir, was this: I think it was about 1938 when the Soo Line, the old company, went into bankruptcy, and when it did so it defaulted on its three issues of bonds. Now, there were guarantees of interest under this agreement of which Mr. Liddy has spoken, and when the default occurred the company was called upon to pay the interest under its guarantee, and as the bonds matured -- there have been two of the issues, of the very large issues, that have matured -- the guarantee came to an end. There was litigation about that, but we succeeded and the guarantee came to an end and the only remaining guarantee is on what are known as the old first refunding bonds, which is really a third mortgage.

THE CHAIRMAN: What became of the litigation?

MR EVANS: We were successful in a number of actions, and then the large action was brought by a number of savings banks and insurance companies which were large holders of these bonds, to have it declared that our guarantee continued until the payment of the principal, and that action never came to trial. The agreed plan of reorganization was formulated between the conflicting parties and the Canadian Pacific, and as a result of that agreed plan of reorganization the action was dropped and the guarantee lapsed on the large issue of first and second mortgage bonds, and remains until at least maturity of the first refunding bonds. There is an elaborate provision in the plan of reorganization for the deposit of these guaranteed bonds and the holding of those guaranteed bonds by a trustee -- it is a very elaborate procedure worked out -- but the plan did not disturb the guarantee so far as there was no dispute up to the point of maturity. There has been no decision on the first refunding bonds.

COMMISSIONER INNIS: The main point would be that you will not in future be involved in any deficit?

MR EVANS: Oh, no, sir, we are not involved in any deficits. There is no further guarantee of the new securities. We will for some little time have to pay something under the guarantee of any first refunding bonds that are outstanding.

COMMISSIONER INNIS: But that will be offset, presumably, by other income from the---

MR EVANS: The earnings on the traffic which we got under that agreement for many years before we were called upon to pay anything under the guarantee.

Q. You have spoken about the matter of the guarantee of interest, and you have also described your view as to the position in regard to the securities of these other companies; does the fact, in your opinion, that the Canadian Pacific has invested some of its earnings in the securities of the new Soo Company change the position at all?

A. No, it does not change the position, Mr. Evans. The investment of the Canadian Pacific and the reorganized Soo Line Company is not included in the Canadian Pacific rail investment, and the earnings received thereon should not be treated as rail income.

Q. Now, there is another one on that exhibit, Mr. Liddy, called the Aroostook Valley Railroad Company; would you give your views as to that?

A. That is the case where the Canadian Pacific Railway Company simply made an investment of some of its funds in securities of the Aroostook Valley. The Canadian Pacific does not include in its rail investment the amounts invested in these securities.

Q. Now I want to ask you about page 27 of the

Appendix to Part I. Mr. Liddy, I notice that that page is in very, very small print; have you got with you some enlarged copies of that statement to assist the Commission in following your discussion of that?

A. Yes, I have some enlargements which may be distributed, Mr. Evans.

MR EVANS: May we have that filed as Exhibit 190? It is the same thing as page 27 of the Appendix, but it will be a little easier to follow on an enlargement.

---EXHIBIT 190: Enlarged copy of page 27 of Appendix to Part I, C.P.R. brief.

MR EVANS: Q. Now, I understand, Mr. Liddy, that in the process of reproducing this page of the Appendix you found that an error was made in the property investment figure in 1948; would you draw the attention of the Commission to that?

A. Yes. The net railway property investment for the year 1948 was shown incorrectly. I believe the enlargements now distributed as Exhibit 190 show the correction in ink. There is also a small correction---

Q. So that figure of 1,031 million odd should be 1,021 million odd?

A. That is right.

Q. Just the change of the digit 3 to 2. And that does affect, I think, also the column entitled "Rate of Return on Net Railway Property Investment", which shows for the year 1948 1.79 per cent; that, I gather, should be 1.8; is that right?

A. That is right.

Q. Now, Mr. Liddy, would you be good enough to comment on this table?

A. This table is an attempt to assemble on one page significant data to indicate the growth and financial record

of the company over 64 years, since 1885, the year in which the first rail connection between Eastern Canada and the Pacific Coast was completed.

Q. Now, what basis did you use in preparing this table, Mr. Liddy?

A. The basis of the figures in this table is the published accounts of the company, adjusted to carry back to past years the effect of current accounting distributions now being made.

Q. Now, what are the most important of those?

A. There are two: First, the distribution of income tax between rail and non-rail; and, secondly, the bringing of corporate and income tax depreciation records into agreement with one another.

Q. That is something you did in 1948?

A. Yes.

Q. As I think you said yesterday?

A. Yes; and that is set out in our 1948 Annual Report to the Shareholders.

Q. That will be found at pages 10 and 11 of the 1948 Annual Report. Now, I notice that the first ten columns on this statement -- Mileage Operated, Net Railway Property Investment, Revenue Freight Ton Miles, Revenue Passenger Miles, Number of Locomotives, Gross Earnings, Working Expenses including Railway Taxes, Net Earnings, Ratio Net to Gross Earnings, and Rate of Return on Railway Property Investment -- have to do with the Canadian Pacific Railway property; and is it right to say that that excludes anything but the railway property, railway operations?

A. That is correct.

Q. Now, I notice that after that Rate of Return column the next column reading from left to right across

the page is "Other Income less Taxes", and am I right that it is in that Other Income that such things as net earnings from ocean steamships, hotels, communications and dividends from say Smelters are included, and that the remainder of the statement after that column, entitled "Other Income", is related to the over-all or corporate position of the company? Am I right in that?

A. That is right.

COMMISSIONER INNIS: This is the income before fixed charges?

MR EVANS: Yes, sir -- well, income before fixed charges you will see is the column next after Other Income, and all the succeeding columns are corporate.

Q. Then were you going to comment on that, Mr.Liddy?

A. Yes, I would like to make a few comments as to the growth of the railway enterprise over the years. This growth can be followed from looking at the figures in the first two columns, which show year by year the mileage of road operated and the amount in dollars of net railway property investment.

Q. That shows, then, that you had to begin with, in 1885, at the end of 1885, approximately 4,000 miles, and thirty-five years later, about 1921, you had about 13,000 miles, and today 17,032.7. Then have you anything to say about the growth in the net railway property investment?

A. Yes. It shows a corresponding growth with the growth of the railway mileage. The Commission will note that the net railway property investment---

THE CHAIRMAN: Pardon me a moment, so I won't go astray. 1948, the mileage is given as 17,000-odd.

MR EVANS: Yes.

THE CHAIRMAN: Does that include leased lines?

MR EVANS: Mileage operated would include leased

lines operated, yes.

THE CHAIRMAN: There is an item of over 9,000 miles in one of the other exhibits, of leased lines; are they included?

MR EVANS: Yes. They are operated by the Canadian Pacific. This is mileage operated by the C nadian P cific.

THE CHAIRMAN: Yes, I see. I thought the total mileage was greater than 17,000.

MR EVANS: Not greater than 17,000. You perhaps should distinguish -- you may hear a greater figure in relation to miles of track. Mr. Liddy is quite familiar with that distinction.

(Page 16744 follows)

THE CHAIRMAN: There is a distinction between miles of track and mileage operated?

MR. EVANS: Yes, because if you have double track you would count it twice to get the miles of track.

THE CHAIRMAN: You only count it once to get the miles operated?

MR. EVANS: Q. Am I right, Mr. Liddy?

A. Yes, mile load is irrespective of whether it is double or single track.

THE CHAIRMAN: The figure you gave the other day was mileage 9,000 for leased lines operated under contract, that does not mean miles of track?

MR. EVANS: I have forgotten the figure. I think what your lordship is referring to is the summary of mileage operated, appearing on page 2 of the Appendix to Part I. You will see there mileage operated, and miles of track. We have there "miles of all tracks: first main track - other main tracks - industrial track - yard track and sidings", with a total of 23,664.

THE CHAIRMAN: In that respect, 13,682 miles was your own?

MR. EVANS: Yes, that is miles of track.

THE CHAIRMAN: And 9,203 miles you did not own, but you operated under lease or contract?

MR. EVANS: Yes.

THE CHAIRMAN: When you come down to the other way of looking at it, that is miles operated, how would those figures compare?

MR. EVANS: The mileage operated?

THE CHAIRMAN: You reduce both of those figures, the 13 and the 9?

MR. EVANS: Yes.

THE CHAIRMAN: Can you tell me how the 17,000

would be divided as between your own mileage and leased mileage or contracted mileage?

MR. EVANS: I would be glad to give you that.

Q Mr. Liddy, have you a figure dividing the miles of road shown in the first column of this Exhibit 190, as between those owned and those operated under lease?

A. Yes, Mr. Evans, that is given in our report to the Dominion Bureau of Statistics.

THE CHAIRMAN: Q. You are getting that, Mr. Liddy, are you?

A. Yes. I was referring, Mr. Chairman, to Exhibit 183, Schedule 24B.

THE CHAIRMAN: I think, Mr. Evans, that the information I wanted is here on page 2. There you have the owned first main track, 9,528, and operated 7,000.

MR. EVANS: Yes; I did not realize that miles of track and first main track meant the same thing.

THE CHAIRMAN: Yes; that is the answer to my question.

COMMISSIONER INNIS: Have you any calculation, Mr. Evans, as to the rate of return including other income, let us say the percentage?

MR. EVANS: I should think it would be quite easy to calculate it, because we have the rate of return -- I suppose that excludes some of the -- we could give it to you.

Q. Have you got a figure showing the rate of return earned on the entire corporate investment from the entire corporate income of the company?

A. No, we don't usually produce that figure, Mr. Evans, because some of the other investments are not based on cost, such as railway investment is. I don't think I have ever seen a figure like that for any railway. It is

quite unusual to do it, Dr. Innis.

COMMISSIONER INNIS: Q. My point would be made by simply adding the net earnings to other income,less taxes, and then the rate of return on railway property. I think you have something else in mind?

A. Yes.

MR. EVANS: He would have to add up the investment on all these things.

THE WITNESS: Your investment is never a firm figure; it is something you buy and sell; whereas, railway property, you have the same figure in cost.

MR. EVANS: Q. Would you deal with the column entitled "Revenue freight ton miles", that is, the third column of figures on Exhibit 190?

A. Revenue freight ton miles increased steadily in volume along with the expansion of the railway until 1913, after which, while there was a continued but gradual growth trend, that fluctuated until the outbreak of the second World War.

Q. What you mean is that there was a very continuous up-trend from 1913, and then you began to have recessions, and increases, and recessions again, until 1939. Is that to the end of 1939?

A. Yes, or the commencement -- the endof 1939 -- 1940. Then in 1941 for the first time in the history of the company the gross revenue freight ton miles exceeded twenty billion, and in the eight years, 1941-48, they have averaged twenty-five billion ton miles.

Q. What is that as compared with the average in, we will say, 1928, for instance?

A. That average of twenty-five billion is 40 per

cent greater than the revenue freight ton miles handled in 1928, which was the pre-depression peak year.

COMMISSIONER INNIS: The figure in 1947 is not very clear on this copy. Is that 20 or 26?

MR. EVANS: Mine is a little blurred too. It looks like 26.

Q. Mr. Liddy, have you got that cleared up on your copy, the figure as to revenue freight ton miles for 1947?

A. I think 27 billion is correct.

Q. Would you deal next with the column headed "Revenue passenger miles."

A. Revenue passenger miles reached record breaking levels in the years 1942 to 1945; but it may be a significant commentary on the railway passenger traffic, that in 1947 and 1948 when we were operating the 17,000 miles of road the revenue passenger miles were back to the 1910-1920 levels, and were actually less than in 1913, at which time we had 11,000 miles of road.

Q. The next column is number of locomotives. Would you like to comment on that?

A. It may be noted that the unprecedented traffic volume of 1941-48 was handled with fewer locomotive units than were operated in any of the twenty-five years prior to 1939.

Q. How has that been accomplished?

A. That was the result of improved methods of operation, larger units and more efficient types of units.

COMMISSIONER INNIS: What is the explanation of the constant figure from 1915, 1916 to 1927?

MR. EVANS: Q. What explanation is there for that, Mr. Liddy? I notice that too.

A. In that period we were on renewal accounting for equipment, and we did not retire any locomotive unless

we had a new one coming along to take its place. The result, incidentally, was that we had some locomotives placed on spare tracks, the parts of which could have perhaps been used as second-hand materials. I might say that was one of the reasons we abandoned renewal accounting for equipment; it inclines to paper railroading.

THE CHAIRMAN: Q. You had been using renewal accounting up to what date?

A. Up to 1930.

MR. EVANS: Q. When you say "paper railroading" you mean a reluctance to retire a unit and have a charge to expense or replacing it in a certain period of time?

A. Yes.

Q. Is that what you mean by "paper railroading"?

A. It has that inclination, yes, Mr. Evans.

THE CHAIRMAN: Q. What do you do with the cast-offs?

MR. EVANS: Q. What do you do with cast-off locomotives when you retire them?

MR. FRAWLEY: Send them to the Northern Alberta railway.

THE WITNESS: We dismantle these locomotives and make use of any second-hand parts that are salvageable; of course steel can always be sold as scrap.

THE CHAIRMAN: Q. You do not keep them for use?

A. Oh, no; once they have been retired from service they are immediately scrapped.

MR. EVANS: Q. I suppose you have some marginally used locomotives which you keep only for peak movements or something of that kind?

A. Yes; in ordinary times there are marginal locomotives. Traffic is never uniform in volume, and

there are times when you have to store these locomotives in what is called, in railway parlance, under white lead.

THE CHAIRMAN: We will take a few minutes recess.

---Recess.

(Page 16749 follows)

... UPON RESUMING

MR. EVANS: Now, you last dealt, Mr. Liddy with the item headed "Number of Locomotives". Now, would you next deal with the four items entitled "Gross Earnings", "Working Expenses Including Railway Taxes", "Net Earnings" and "Ratio Net to Gross Earnings"?

A. It is significant that during one half of the railway's history, the ratio of net to gross ranged generally between 30 and40 per cent.

Q. Now, you are looking down the column to the period ending with about 1917, am I right in that - perhaps 1916?

A. Yes, about that period, Mr. Evans.

Q. And throughout that period you say, that the ratio of net to gross was upwards of 30 per cent?

A. That is right.

COMMISSIONER ANGUS: The item "Railway Taxes" includes what taxes?

A. That includes municipal taxes, provincial taxes and railway income tax so computed as applying to the railway in contra-distinction to income tax applying to Other Income.

MR. EVANS: Now then, what about the period subsequent to 1918 on ratio of net to gross?

A. Subsequent to 1918, the ratio has been less than 20 per cent, and for the years 1946, 1947 and 1948, the ratio has been less than 10 per cent.

Q. That is, notwithstanding the large increase in gross earnings that was experienced in those years?

A. Yes, notwithstanding that fact, Mr. Evans. In 1948, the gross earnings and working expenses were

$355 million and $336 million respectively.

Q. That is to say, earnings were over $355 million, the expenses were over $336 million, and yet you point to the ratio of net to gross of 5.18 per cent?

A. That is right.

Q. The ratio is 5.18?

A. Yes, that is slightly less than 5 cents out of each dollar the railway earns.

Q. I think it is a little more to be accurate.

A. Yes, slightly more.

Q. About 5 1/5 cents or thereabouts?

A. Yes.

Q. Now then, the next column after the ratio of net to gross, is the "Rate of Return"?

MR. FRAWLEY: My lord, before Mr. Evans discusses this, I do not want for a moment to revive yesterday's discussion. I merely would like it on the record that we do not accept that figure "Rate of Return on Net Railway Property Investment" as truly disclosing the rate of return because, of course, we challenged the second column "Net Railway Property Investment".

Now, we were heard on that point yesterday, and I merely want to make it clear this morning that we still maintain that position, and, therefore, this "Rate of Return" column that my friend is going to discuss, is not the rate of return for rate fixing purposes that my friend is using it for.

THE CHAIRMAN: Do you mean to tell me then, that we have already heard all that you and others intend to bring to us against this?

MR. FRAWLEY: Your lordship has not heard all we have to say on the question of the rate base and rate of

return, but I do not want our silence this morning to indicate that there was no change in our attitude of yesterday.

THE CHAIRMAN: Your silence is without prejudice?

MR. FRAWLEY: Yes, sir, yesterday and today and forever.

MR. EVANS: Now, Mr. Liddy, under this cloud that Mr. Frawley has put upon us, would you please comment upon this column entitled "Rate of Return on Net Railway Property Investment"?

A. That column shows a rate of return exceeding 7 per cent for the year 1912.

Q. That is, 7.28 per cent in 1912 - yes?

A. A rate exceeding 6 per cent in the years 1910, 1911, and 1913.

Q. Now, that figure of 7.47 in the six months ended December 31, 1916, I suppose, is a half-yearly figure? You see that figure of 7.47?

A. Yes, that is a half year, Mr. Evans.

Q. Now, then, what happened to that rate of returnn in subsequent years?

A. I would like to point to the years in which the rate of return was about 5 per cent. They were the years 1906 - -

Q. That is 5.81.?

A. 1907.

Q. 5.94 .

A. 1914.

Q. 5.26.

A. 1916 - -

COMMISSIONER INNIS: Are you excluding thnis 6?

THE CHAIRMAN: You passed over the years that

produced more than 6 per cent.

MR. EVANS: I think the witness mentioned one year that produced over 7 and then he mentioned several years that were over 6.

THE CHAIRMAN: Now you are on the years between 5 and 6?

MR. EVANS: Yes.

MR. FRAWLEY: Coming down the toboggan?

MR. EVANS: We certainly are on the skids, Mr. Frawley.

MR. FRAWLEY: You got pushed back up this morning.

THE WITNESS: Then there was the year 1917, Mr. Evans - 5.24 per cent, and the year 1943, 5.18 per cent.

MR. EVANS: Now, have you anything further to say about that column?

A. I would like to draw attention to the year 1948, when the return on net railway property investment was only 1.80 per cent.

Q. Now then, turning to the column entitled "Other Income" - -

COMMISSIONER INNIS: Before you leave this Table, I hope I won't precipitate a further controversial discussion, but it would seem that the wide range in the rate of return would indicate that net railway property investment was not a very satisfactory possible rate base. Now, I do not want you to become involved in further controversy.

MR. EVANS: Would you like me to comment on it?

COMMISSIONER INNIS: Yes, I would.

MR. EVANS: I will try to not start a roar behind me. I think it is fair to say, that by and large the net property investment rate base, leaving aside my friends'

challenge about what is in it, and what is out of it, is the basis which the United States regulatory bodies have come to adopt.

Now, it began in a very different way. My friend, Mr. Smith, yesterday, referred to the doctrine in the United States Constitution out of which grew the decision in Smyth v Ames. Now, that was simply this, that you might not take, as it were, the property of a utility and devote it to the public use and through regulation prevent that property from earning a fair return. Now, in Smyth v Ames, it was laid down, that you ought perhaps to look at,as well as the original cost,the cost of reproduction, and I think there is also in one of the Statutes, one of the State Statutes, a provision that the return is to be figured on reproduction cost.

The Interstate Commerce Commission made a valuation and have kept that up to date on a reproduction cost basis until about two years ago. They may still keep the figures. They, for many years, allowed a rate of return based on an average of the depreciated cost basis and the reproduction cost less depreciation, and so up until Ex Parte 166 that was the basis on which the Interstate Commerce Commission went.

Now, in a long series of cases which followed Smith v Ames, the doctrine of reproduction cost was pretty well tossed overboard. I think my friend Mr. MacPherson is the author of a statement in the proceedings before the Board that the ghost of the case of Smyth v Ames was laid. The ghost that was laid was the ghost of reproduction cost.

Now then, I think it is a fair summary to say, and I gave the Commission a reference to Mr. Priest's argument, that by and large the principle is a depreciated investment

base or a depreciated historical cost base. Now, it may have its short-comings. Some people think it has; some people think it should be reproduction cost; other people think that the difficulty of getting a reproduction cost is so great as to remove any practical value from that sort of thing. We know that the American railway valuation took fifteen or twenty years as a minimum and it is coming down to looking at what practically is valuable for the purpose of providing a rate of return. We think it is a practical basis.

COMMISSIONER INNIS: I was wondering whether the indications of very wide fluctuations in your Exhibit 188, as well as the very wide range indicated in these figures running from 1.80 to 7.47, may not suggest that in Canada the problem of variability of traffic would mean, that adherence to net railway property investment would produce wide rigidities?

MR. EVANS: Well, I agree with you to this extent, that if you were to say to a railway company: "We will guarantee you so much on your property investment" that that would provide those rigidities. The experience with that is rather interesting, because in the Transportation Act of 1920 in the United States there was a provision that the regulatory tribunal, the Interstate Commerce Commission, should permit the railways in that country to earn a return of 5½ per cent. While you might permit one railway or ten railways to earn 5½ per cent, if the law requires it to be common to all of them, you could never guarantee that the smallest or poorest railway would get 5½ per cent.

Now, we can quite see that you cannot guarantee a return, but my submission would be that the regulatory tribunal when it is asked to increase rates could give

permission to increase rates to permit the Company to earn a return as high as that. In other words, they would not operate to reduce rates if the return fell below a certain figure, but I would not suggest for one moment that a regulatory tribunal could guarantee in good times and bad that a return would be X per cent, no more and no less.

THE CHAIRMAN: When you use the word 'guarantee", what do you mean?

MR. EVANS: I thought perhaps it was implicit in Dr. Innis' question that there was something rigid in the rate of return and that that might not be possible in view of the acknowledged fluctuations that have been general over a period of years.

COMMISSIONER INNIS: I wonder if it would be possible for the Board to work out a formula which would admit of such fluctuations in the rates as seem to appear?

MR. EVANS: Well, as a practical matter, sir, wouldn't it amount to this, that the railways would go to the Board asking for an increase in rates, and if the increase in rates asked for would not produce greater than the return which the Board thought was fair on the investment, the application would be granted. Now then, if the railway did not obtain the revenue that it thought it was going to obtain, it might drop down a little bit, or, in specially good times, it might go up, but there would be no rigid adherence, no guarantee, for instance, that in depression times the railways would have to have that return. In their own interests they probably would not want to go and ask for an increase in rates that would give them a specified return in a period of depression.

COMMISSIONER INNIS: But you would need a Board -

I won't say omniscient, but one which followed very closely the whole problem of traffic, net earnings and so on?

MR. EVANS: I wonder if you do, sir. You take a given situation. Let us suppose that this Board in the Judgment handed down today, had suggested that you might increase rates X per cent, and that when rates were increased that that would provide a return of Y per cent on the investment, and that they deemed that fair and reasonable. Now, it would not follow at all, that they would have to be omniscient, because if the return went up, we will say in 1950 - suppose they allowed 6 per cent and the return went up to $7\frac{1}{2}$ or 8 per cent they would just step in with an order to reduce rates.

(Page 16760 follows)

The principle is exactly the same whether you are going on requirements or going on rate of return. The requirement principle is that you earn so much money, while the return on investment principle is that you earn so much money, only you calculate---

THE CHAIRMAN: Then this would be a sort of yearly revision, would it?

MR EVANS: I think that is inherent and implicit in any method, whether you go on requirements or on return on investment, because, after all, the return on investment can be calculated and will produce a certain number of dollars. Now, it does not make any difference how you arrive at the number of dollars you are going to be permitted to earn, you still have that problem.

THE CHAIRMAN: Are we concerned with the prevailing capital rates on the market in attempting to work out what is needed?

MR EVANS: Oh, yes. Then, of course, in determining what the permissible return would be, they would have regard to the conditions of the market. That would have to be established in evidence. We did do that in the 20% Case; we did give a lot of evidence about the amount of return necessary to attract capital. There were a large number of exhibits showing trends of prices of stocks and what they yielded, how they were selling, what yield basis they were selling at. There was a very large number of exhibits.

COMMISSIONER INNIS: Would not the Board almost certainly move into the next step, that is to say, considering the sort of securities which would be used? If you were to depend on common stock, as I presume would be the case with the Canadian Pacific, it would be a vastly different situation than one in which you were, say, dependent

on bonds.

MR EVANS: Yes, I think so; but I think that there is pretty well a rule of thumb for that too. There was evidence by Mr. Northey Jones in the 20% Case on that very subject. He expressed a very definite opinion that it was desirable to keep the ratio of debt to total capitalization below 50 per cent, and on that basis he calculated his rate of return on a theoretical capital structure. That certainly can be done, but I would not ask any board to make a rigid determination for all time, under all circumstances, of a certain rate of return, and to guarantee that to us in all circumstances.

COMMISSIONER INNIS: I am just worried as to the sort of problem that is being imposed or being placed before the Board in a country in which fluctuations are so wide.

MR EVANS: Well, as I say, the same problem arises whether you go on requirements or on return on investment, because your ratio here is derived from the net in relation to investment, and if the net fluctuates, as it will do, you have still got a fluctuation even if you go on a requirement basis.

COMMISSIONER INNIS: I am sorry to have taken so much time.

COMMISSIONER ANGUS: May I follow up that question by this one? Do you attribute the wide fluctuations of the figures in this column to the fluctuating character of the railway business as an enterprise, or do you think that they result in part from rigidities in applying rate controls -- I mean in allowing increases when they are desirable and making decreases when they are desirable?

MR EVANS: I do not think you could say any one factor. I would think that increases in unit costs, in-

creases in wages, changes in rates, changes in competition -- almost an unlimited number of things -- could affect that ratio. Perhaps I have not followed you.

COMMISSIONER ANGUS: Do you consider that the spread between the fat years and the lean ones is greater than it should be if you had, shall we say, a more responsive system of rate regulation?

MR EVANS: Well, I do think so to this extent -- perhaps not altogether, but let me take the first case. If you speak of the period from the twenties to the thirties, you might quite properly expect quite a wide fluctuation; but, on the other hand, to find in a period of very high traffic volume a downward curve in the return would indicate that there is too much time consumed between the application for relief and the granting of relief. That has certainly been one of our greatest problems.

THE CHAIRMAN: Have you anything specifically to suggest about shortening that time?

MR O'DONNELL: Forbidding Mr. Frawley from going into those cases.

THE CHAIRMAN: I do not mean the extermination of your opponents at all.

MR EVANS: I would not want to exterminate them, but I would hope in the course of time that our motives and our needs would be better understood by our friends, and I think that if that should take place much of our difficulty about lapse of time would have disappeared.

MR FRAWLEY: When Mr. Evans understands our needs we will understand his. That has been his trouble all through the years.

MR EVANS: I thought I made a very fair retort to the Chairman, Mr. Frawley.

MR MACPHERSON: I think, Mr. Evans, that it should be added, perhaps, that there was evidence led by the C.P.R. in the 20% Case as to rate base and rate of return. Rate base was suggested as one-billion-one. The evidence of Dr. Dorau was that a fair rate of return would be 8.2 per cent.

MR EVANS: Yes, a fair rate of return would have been 8.2 per cent, according to Dr. Dorau.

COMMISSIONER INNIS: That is 8 per cent on the net railway property investment.

MR MACPHERSON: That was what was asked for, and I will be glad to file with you an exhibit put in at that time and acknowledged by Dr. Dorau which would indicate the extent to which freight rates would have to be raised in Canada to produce that.

MR EVANS: Well, that is a very interesting interjection of Mr. MacPherson's, because his sole cross-examination of Dr. Dorau had nothing whatever to do with his evidence, but as to how he would raise the money, which was not a matter of concern to Dr. Dorau, because he had no idea, and Mr. MacPherson put in an exhibit showing what increase in rates would have been necessary to give effect to that 8.2 per cent return.

COMMISSIONER INNIS: The figure of 8.2 exceeds anything in this whole table.

MR EVANS: Yes, sir, but of course the investment is stated in dollars of a different value from the return being paid. He put in an exhibit -- as a matter of interest; I am not arguing this question, but I think perhaps it would be informative -- he put in an exhibit in which he did what was called the vintaging of the dollars; in other words, he took a dollar spent we will say in each of the several years, and he related that to its present-day purchasing power; as

increments of capital were added he expressed those in terms of present-day value of the dollar; and by that process he got a figure of $1,800-odd million as the present-day value of the property, by taking the dollar value in terms of what it would purchase today. So it was certainly implicit in his evidence that the return expressed as a percentage of an original dollar cost base would have to reflect the difference in the value of the dollar. It is a very different thing if you can go to a reproduction cost base, because when you go to a reproduction cost base you express your base in terms of present-day dollars, and you therefore can express your return as a percentage of that in present-day dollars, and you get a very much smaller percentage return.

Q. Now, Mr. Liddy, we were going to ask you to deal with the column in Exhibit 190 headed "Other Income less Taxes".

THE CHAIRMAN: Where do we find the list of the sources from which this Other Income is derived?

MR EVANS: Well, there is no list in this case.

THE CHAIRMAN: I thought perhaps some of the other exhibits would have shown it.

MR EVANS: The Annual Report is the only source I know. There were exhibits filed in the rate cases showing the principal sources.

THE CHAIRMAN: But the Annual Report will show those?

MR EVANS: It will show a very large number of them. There are some what we call basket items, miscellaneous items., but the Report does show the principal sources.

COMMISSIONER INNIS: You have not actually, or are you puttiing in as an exhibit the extent to which labour is responsi.ble for the working expenses?

MR EVANS: We did before the Board of Transport Commissioners. We had exhibits, and they can be referred to; I will look them up and give you a reference to them. Both railways, ourselves and our friends the Canadian National, did the same thing.

Q. Now, Mr. Liddy, if you would deal with that question of Other Income less Taxes?

A. Yes. Other Income shows a modest beginning in 1892 with earnings of $33,201. Earnings of from $8 to $10 million were usual occurrences up until 1945.

Q. Let us just follow that down the column. $8 to $10 million, that apparently begins about 1914 with $8.5 million, and then with rare exceptions it was more than that down to and including 1931; is that correct? There was only one year in between 1914 and 1931 where it fell below your $8 million?

A. Yes.

Q. And then following that?

A. Then we have the period of the depression, in which Other Income declined drastically. Then we come to the period 1946-47-48, in which income of $16, $20 and $24 million is shown, and that is as a result largely of the prices obtained by the Consolidated Mining and Smelting Company for base metals.

Q. That enabled them to pay a higher dividend?

A. Yes.

Q. Now, the next column is Income before Fixed Charges; have you anything to add?

COMMISSIONER INNIS: This column fluctuates even more widely than the Net Earnings.

MR EVANS: Yes.

THE CHAIRMAN: Before you discuss Income before Fixed charges, will you let me know what you include Fixed

Charges on, in the next column?

MR EVANS: Q. Mr. Liddy, the Chairman would like to know what you include in Income?

THE CHAIRMAN: Not in Income; the next column; these Fixed Charges are Fixed Charges on what?

MR EVANS: Oh, I see. There may be a legal connotation in your question.

MR MCLEAN: I think it is a practical connotation as well as a legal one, sir.

THE CHAIRMAN: Oh, yes, it is.

MR EVANS: I did not mean to exclude that. I don't know what is wrong with my friend Mr. McLean.

THE CHAIRMAN: Well, it is a matter of fact, you see, too, because you say "Fixed Charges".

MR EVANS: They are the fixed charges of the company, of the Canadian Pacific Railway Company, and they consist, sir, of charges, mainly interest on the consolidated debenture stock. The consolidated debenture stock is what is known as a floating charge; it is not a fixed charge on any particular assets; it is a statutory charge much in the nature of a floating charge. It does not crystallize and attach to assets until default occurs. Now, unlike most floating charges, our consolidated debenture stock never attaches even on default. The right of a holder of consolidated debenture stock is to vote in lieu of the common or ordinary stockholder's right to vote; that is to say, if we were to default on the debenture stock, the right of the ordinary stockholder to vote ceases until the default is made good, and the debenture stockholder acquires the right to vote. Now, that is by far the greatest amount of outstanding fixed charge that the company has.

COMMISSIONER INNIS: That is related to your third column from the end.

MR EVANS: Yes; I had forgotten that that is on the exhibit -- the long term debt. Your lordship will see that in 1948 there is $295,438,229 of that perpetual 4 per cent consolidated debenture stock outstanding. The next column shows the bonds, notes and equipment obligations. Now, perhaps I could give you a bird's eye view of the position with regard to those. The equipment obligation, as I think I explained some time back, is an obligation to pay off to a trustee the remaining purchase price of equipment the title to which is held by the trustee until it is paid off, so that in that respect that obligation, that equipment obligation, is a security on equipment, a specified equipment, not generally but specific equipment, the title to which is held by the trustee, and the equipment is operated by the company under lease. Now, the bonds---

THE CHAIRMAN: Pardon me. Then can I take it that you then relate this column of fixed charges entirely to these other two columns, long term debt?

MR EVANS: Yes -- well, no; there are some other items.

THE WITNESS: Rent.

MR EVANS: There are some rentals under leases. I was going to give you, perhaps, a bird's eye view of what these consist of.

THE CHAIRMAN: That is all right; I am following you.

MR EVANS: Before we leave that column, bonds, notes and equipment obligations, we have no bonds that are fixed charges on specific assets -- the company has not. They have bonds secured by deposit of this same debenture stock. There are a few of those left. Now, some of the lessor companies who have leased to us certain lines have

bonds on their properties. They attach to the leasehold property. But the Canadian Pacific has no bonds attaching to specific property.

THE CHAIRMAN: Do you take over any liability on the bonds of these companies?

MR EVANS: We agree in the lease to pay the interest on the bonds, and sometimes a dividend on the stock.

THE CHAIRMAN: I see.

MR EVANS: But if there were default the bonds would attach only to the leasehold property and not to the other property of the company.

THE CHAIRMAN: Yes, I understand.

MR EVANS: Does that help your lordship?

THE CHAIRMAN: Oh, yes.

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MR. EVANS: Q. Now, Mr. Liddy, you were about to comment on income before fixed charges?

A. Yes. On the basis of this statement the income has been sufficient to meet interest and rental charges in all years, excepting those of 1888, 1894, and the four years 1932-35.

Q. Now, would you have something to say about the next column, fixed charges?

A. The fixed charges increased progressively until 1938, when they amounted to $26,863,132.

Q. That was the peak?

A. Yes, that was the high point of fixed charges. The rate of interest paid on consolidated debenture stock, which is the largest item, comprised in our fixed charges, is 4 per cent.

Q. What is the average interest rate on equipment obligations?

A. For the year 1948 the average was 2.06 per cent.

Q. And the interest rate on bonds -- those are collateral trust bonds, I presume?

A. Yes, they were collateral trust bonds. The interest on those averaged 3.72 per cent.

COMMISSIONER INNIS: Q. How do you explain the rather sharp fluctuation say from 1929 to 1948, in the bonds, notes and equipment obligations? Does that mean you exercised very close control over the fixed charges arising from those items?

A. We used our entire net earnings and other income to reduce the debt from 1939 to 1943. We didn't pay any dividends in all those years, but applied all our surpluses, all our cash, to reducing the debt.

MR. EVANS:Q.That I think shows itself under the two columns, dividends declared?

A. Yes; you can see the void there in that period of dividends --

COMMISSIONER INNIS: Q. Did you say from 1939?

MR. EVANS: 1932 --

MR.COVERT: Perhaps there is a misunderstanding. I understood Dr. Innis' question was from 1929 there was a sharp fluctuation; in 1929 the trust bonds outstanding were 124, and they go up in 1933 to 202. That is an increase.

COMMISSIONER INNIS: 222.

MR. COVERT: That was your point?

COMMISSIONER INNIS: Yes.

THE WITNESS: I misunderstood the question; I thought you were speaking of 1939.

COMMISSIONER INNIS: Q. No, 1929.

A. The increase that occurred on bonds, notes and equipment obligations outstanding from 1929 to 1939 is a reflection of the fact that the company found difficulty in going into the money markets to float capital stock issues, and had to rely upon issuing bonded debt securities; and then after that period, that is after 1939, as I have explained, the company applied its entire resources to their reduction of debt.

Q That would be a definite depression policy?

A. Well, it was a reflection, I would think, Dr. Innis, of the low rate of return we were getting.

Q. It was something which you had to meet by relying on that type of security?

A. That is right.

Q. The interest rate during that period would vary, of course?

A. I think it increased. I haven't got the figures in front of me, but I do remember in 1933 and

1934 we had to pay 5 per cent interest on short-term issues.

Q. That was in the depression?

A. Yes, sir.

MR. EVANS: Q. Wasn't there a time in the depression when you had to sell some securities, some 6 per cent securities, at a discount? Was there not something of that kind mentioned by Mr. Unwin?

A. I think I do recall a case like that, Mr. Evans, but we were not successful even issuing very many of those securities.

COMMISSIONER INNIS: Q. But those were all short-term securities?

A. Yes.

Q Because you kept your position movable?

A. Yes. We have at the present time practically liquidated our fixed obligations outstanding, apart from our leased line obligations, of course.

MR. EVANS: Q. And I assume there is some equipment still outstanding?

A. Yes; there is a substantial amount of equipment outstanding.

COMMISSIONER INNIS: Q. When you say you have practically wiped it out, does that mean that the 1949 figure would be very much less?

A. At December 31, 1948 -- I am now looking at the company's annual report -- there were three collateral trust bond issues outstanding, amounting to approximately $34 million; the 4 per cent issue matured July 2, 1949, and has been paid off, leaving only two issues of 3½ per cent interest rates of $13,500,000 outstanding.

MR. EVANS: Q. Where did you get the money to pay off that collateral trust bond issue, as a matter of interest, Mr. Liddy?

A. The $10,700,000 issue that you referred to, Mr. Evans, was largely paid off, or perhaps wholly paid off, by utilizing a steamship replacement fund.

THE CHAIRMAN: Q. Did you say a steamship replacement fund?

A. A steamship replacement fund; that is vessels we lost during the war, which the British Ministry paid us for.

MR. EVANS: Perhaps my friend would appreciate the extent of that gift, the reduction in fixed charges that has been obtained.

THE CHAIRMAN: You did not build any ships?

MR. EVANS: No, but we had the money put in a fund for the building of ships, and we paid off fixed charges.

Q. Had you finished dealing with income before fixed charges? Then fixed charges. Now, on dividends, have you any comment you want to make?

A. Dividends on preference stock at the rate of 4 per cent have been paid in every year since preference stock was first sold, except during the depression years of the 1930's, when only partial dividends or no dividends at all were possible.

THE CHAIRMAN: Q. Those figures precede what appears to be the letter "D"?

A. No, I am on the next column, Mr. Chairman.

MR. EVANS: They appear to be about the same year.

THE CHAIRMAN: They are preference; I was looking at the wrong column.

MR. EVANS: Q. There were three years, 1933, 1934 and 1935, when no preference dividends were paid at all, and then a lower dividend rate in 1936, then lower but somewhat higher than the previous year was paid in 1937. Then none in 1938 and 1939, is that correct?

[illegible] ment [illegible]

[illegible] that is [illegible]

the subject of the [illegible]

[illegible] ships [illegible]

[illegible] but [illegible] the more [illegible]

[illegible] building of [illegible]

[illegible]

[illegible] 1934.

A. That is right.

Q. Then in 1940 they resumed the full payment of preferred dividends?

A. That is right; and it has been continued since that time.

COMMISSIONER INNIS: Those are 4 per cent?

MR. EVANS: Yes.

Q. That isn't accumulative preferred stock?

A. No, it is non-cumulative.

Q. Then coming to the ordinary stock dividends.

A. The dividends on ordinary stock have been irregular over the years, except for the period 1911 to 1930, when the annual dividends of 10 per cent were paid, 7 per cent being declared from railway earnings and 3 per cent from other income.

Q. Now during the eleven years, 1932 to 1942, there was, I gather from this, no ordinary dividends at all?

A. That is right. Dividend payments on ordinary stock were resumed in the fall of 1943, and have since been maintained on the 5 per cent basis.

COMMISSIONER INNIS: Did you have difficulty selling the consolidated debenture stock after the 1932 period?

MR. EVANS: Oh, my, yes. That is why they developed this device of the consolidated trust bonds.

Q. Am I right in this, Mr. Liddy, that during that period you had to, on those bond issues, provide a specified rate of coverage of the security, up to a certain market value of the consolidated debenture stock. Do you remember that?

A. Yes. Perhaps a little excerpt from the 1933 annual report would be informative, Mr. Evans. I quote

from page 9:

"Owing to continued unfavourable conditions of the financial market, no capital stock or consolidated debenture stock was sold during the year. For the purpose of retiring obligations maturing in 1933 and 1934, your company borrowed from the Canadian banks the sum of $60 million. . ."

and so on; the history of that is pretty well known.

Q. I was thinking particularly of the consolidated trust bonds, when they were issued during the depression. You had to keep putting up more and more security; they were secured by the consolidated debenture stock. Isn't it a fact that more and more debenture stock had to be deposited to give the necessary security?

A. I am not very familiar with that personally, I am sorry, but I do know that the collateral that was necessary to be put up was substantial.

COMMISSIONER INNIS: Then these fluctuations which we spoke of earlier, 1929 to 1940, are closely related to this marketing of consolidated debentures.

MR. EVANS: What year?

COMMISSIONER INNIS: The point we were discussing earlier, 1929 to 1939. Those fluctuations are closely related to this problem of the inability to handle the consolidated debentures?

MR. EVANS: Q. Can you answer that, Mr. Liddy?

A. Well, I think some of the difficulty with consolidated debenture stock is, sir, it is largely held in Great Britain, and it is an old country favourite stock; all that market has been, as you know, restricted; as a matter of fact, it is closed.

COMMISSIONER INNIS: Q. But that fact is registered in your second last column, bonds, notes and equipment?

[illegible] want you [illegible]

[illegible]

[illegible] stock was [illegible]

[illegible] getting [illegible]

[illegible] your company [illegible]

[illegible] the [illegible]

[illegible] that is pretty [illegible]

[illegible]

A Yes, bonnd to have an effect.

MR. EVANS: What Mr. Liddy has in mind is in order to sell debenture stock as such, there would have to be deposited as security for some of these bonds in the column entitled "Bonds, notes and equipment obligations" a considerable amount of debenture stock which is not taken as issued until default should occur.

THE CHAIRMAN: We will adjourn now.

--- The Commission adjourned at 1.00 p.m., to meet again at 2.45 p.m.

Wednesday, March 1, 1950

AFTERNOON SESSION

S. J. W. LIDDY, recalled:

Examination continued:

BY MR. EVANS:

Q. At the adjournment, Mr. Liddy, you were about to deal with the columns on Exhibit 190 headed "Capital Stock". Would you now proceed to discuss those two columns?

A. Yes. I would like to refer to the capital stock for the year 1948, consisting of $137,256,921 of preference, and $335,000,000 of ordinary stock; that is, a total of preference and ordinary of $472 millions odd.

Q. Now, what about the long term debt compared with that?

A. For the same year, the long term debt, consisting of $295,438,229 of perpetual 4 per cent consolidated debenture stock, and $102,037,000 of bonds, notes and equipment obligations; they total, those two captions, to the sum of $397,000,000-odd.

The point I want to bring out is: the proportion of capital stock --

THE CHAIRMAN: What did you say those figures were again?

A. $102,037,000 for bonds, notes and equipment obligations; and $295,438,229 for perpetual 4 per cent consolidated debenture stock.

MR. EVANS: Q. You were going to tell us about the proportion of stock to debt?

A. Yes. The proportion of capital stock to long term debt thus works out to a ratio of 54 to 46.

Q. Yes. And how does that compare with what it was thirty years before, let us say, in 1918?

A. Thirty years previously the ratio was around

59 to 41.

Q. And in 1928, let us say?

A. In 1928 it was about the same as it is today, 54 to 46.

Q. Yes. Now, there is a footnote. Would you like to comment on it?

A. Yes. This footnote to Exhibit 190 points out that the capital stock and long term debt are stated at par over the principal amount; and that at December 31, 1948, ordinary stock equity exceeded the par value by $407,587,173.

Q. Perhaps you would not mind just taking a moment to explain what you mean when you say "stock equity exceeds par value by that $407,587,173"? Does that represent a part of a premium on the stock?

A. Another term is the net worth of the stock, the net worth in the company.

Q. Yes. Did the shareholders, over the years, pay par, or more than par for their stock?

A. The ordinary stockholders, over the years, have paid a premium for their stock. Altogether, this premium exceeds $77 million odd.

Q. That is the figure at the end of the footnote?

A. Yes.

Q. And the net proceeds from sales amounted to $77,166,226?

COMMISSIONER INNIS: Q. In what period was the stock sold at a premium?

A. I can get that for you in a minute.

Q. It will be in the period when you were paying 10 per cent dividend?

A. Yes, it would start about then. Prior to that time I believe the stock was sold at a discount.

MR. EVANS: Q. Is this figure of $77 million odd

net premium?

A. That is the net figure, yes.

Q. But the gross premium paid for stock issues was in excess of that; but there were certain stocks which were sold at a discount, which, netted, gives you $77 million odd?

A. Yes. Our first issues of stock were sold at a very heavy discount.

Q. Yes?

A. There was a stock issue in 1883 which was sold at a discount of $15 million.

Q. What par principal amount was that?

A. $20,000,000.

In 1883 there was an issue of $30 million, which was sold at a discount of $14 million.

In 1884 there was an issue of $10 million of stock which was sold at a discount of $5 million.

And from 1903 on, in whatever year there were new issues of stock, they were sold at premiums.

Q. But this figure of $77,166,226 is a netted figure? Am I right? It takes into account the discounts in earlier years as well as the premiums in the later years?

A. That is right.

Q. What have you to say about the current dividend of 5 per cent on the ordinary stock?

A. Taking into consideration the excess of the equity over the par value of Canadian Pacific stock, the current dividend rates of 5 per cent represent a return on book value, including that equity, of approximately 2-1/4 per cent only.

Q. Yes.

COMMISSIONER INNIS: You have not compiled a sort of table?

A. Well, the equity has not changed greatly. It would change over a period of a decade or so, but that would still be true of four or five years previously, the last four or five years.

MR. EVANS: Q. Then we now turn to another subject.

Would you turn to page 3 of the appendix to Part I of the submission? That is a map showing freight traffic density of the Canadian Pacific Railway.

Now, Mr. Liddy, looking at that map, will you please tell the Commission the basis on which that map was prepared?

A. This map, showing the freight traffic density, is calculated on the basis of net ton miles per mile of road for the year 1948.

Q. Net ton miles per mile of road for the year 1948. First of all, what do you mean by "net ton miles"?

A. Net ton mile is the movement in road service of one ton of freight traffic, revenue and non-revenue, over a distance of one mile.

Q. Yes?

A. That is, it includes the weight of the contents only, not the weight of the freight car.

Q. Yes. Now, how many net ton miles of work were performed in 1948?

A. Approximately 27-1/2 billion.

Q. Now, "miles of road"; what do you mean by "miles of road"?

A. Miles of road pertain to the actual distance between termini of lines on the railway on which freight trains are operated.

Q. Are double track lines taken into account in

"miles of road"?

A. No. They are not counted twice.

Q. Now then, how many miles of road were operated in freight service in the Canadian Pacific in 1948?

A. Approximately 17,000 miles of road.

(Page 16783 follows)

Q. Now, with that background, will you tell me how the freight traffic density shown on this map at page 3 of the Appendix, was calculated?

A. The freight traffic density in each direction, that is, east and west, or north and south, has been calculated separately for each section of line for the year 1948 by dividing the net ton miles by the miles of road.

Q. Now, the map, as I gather, shows lines as well as figures in connection with each section. Would you describe those and comment on them?

A. The figures on the map show for each section of line, the freight traffic density in the direction of traffic indicated by an arrow in units of 100 thousand net ton miles per mile of road.

Q. Now, just before you go ahead with that, the figures are quite small, but would you just like to pick out some example, that perhaps could assist the Commission in reading the map?

A. Yes, take the line from Fort William to Ignace, which is shown in the upper right hand corner - -

Q. Yes.

A. The top figure, the figure appearing at the top of the fine lines if I read it correctly, is 25.9.

Q. And then there is an arrow pointing to the left. Does that indicate a west-bound movement?

A. Yes, that is a west-bound movement. Now, the east-bound movement is down at the bottom. I believe the figure is 67.3.

Q. And the arrow, I see there, is on the right pointing in an easterly direction?

A. As would be expected with the grain traffic coming

down from Fort William.

Q. Now then, the lines that are drawn, I see that in that particular section of line there appears to be a very large number of fine lines below the line of railway itself and then a smaller number above. Will you tell me what those lines represent

A. Each fine line indicates a freight traffic density of 100 thousand net ton miles per mile of road.

Q. Now, "net ton miles", as we have understood it before, is the weight of the contents and does not include the weight of the car?

A. Yes, that is correct.

Q. Now, take another section of line. Let us look at Broadview to Regina, for an example. What would that map show with regard to Broadview and Regina?

A. There are ten fine lines etched in above the railway line in the west-bound direction in that section.

Q. In order to let the Commission find that on the map, that is the section of line which appears just right of centre in the upper section of the map, and that also shows, as I gather, a larger east-bound movement than west-bound?

A. Yes.

Q. And what you have said is, that the west-bound lines, that is, above the railway line with the arrow pointing left, there are ten lines each indicating one hundred thousand net ton miles per mile of road?

A. That makes it altogether a million net ton miles in a west-bound direction.

Q. And east-bound - what does that show?

A. East-bound is about four times as great. If my

eyes are correct, it is 41.4. That is a little over four million net ton miles in the east-bound direction.

Q. Now, would you summarize for the Commission the result of an analysis of that map we have been discussing

A. Yes. I would like to group the miles of road, the traffic density in miles of road into three categories, namely, heavy, medium and light freight traffic density lines.

Q. What do you call "heavy density lines"?

A. Those lines having in excess of two million seven hundred and fifty thousand net ton miles per mile of road.

Q. And the medium density lines?

A. Between two million seven hundred and fifty thousand and two hundred and fifty thousand.

Q. That is per mile of road per annum?

A. Yes, sir.

Q. Now then, the light density line s I suppose, would be those below the lower limit of the medium, that is below two hundred and fifty thousand net ton miles per mile of road per annum?

A. That is right.

Q. Now then, where did that grouping of those categories originate as far as you know?

A. This grouping was employed by Commissioner Loree in the 1930 and 1931 Royal Commission Investigation.

Q. I think that will be found on page 41 of the Duff Commission Report if the Commission is interested. Now, will you give the mileage in each of those three groupings you have described?

A. First, the heavy grouping, that is, over two and three-quarter million net ton miles per mile of road, there

were for the year 1948 three thousand nine hundred and twenty four miles or 23 per cent of the total mileage in that grouping.

Q. That is road miles, not track miles?

A. Per mile of road, that is right. In the second category - -

Q. That is in the medium group?

A. Yes, there were six thousand one hundred and fifty eight miles or 36%.

Q. And in the third category, the light traffic?

A. There were six thousand nine hundred and one or 41%.

Q. Now, have you got a figure of average density of Canadian Pacific lines east and west?

A. Yes. On this same basis, the average in ton miles per mile of road lines east for the year 1948 was two million and nineteen thousand and lines west one million four hundred and eight thousand, and the system average was one million six hundred and fifteen thousand.

Q. Always speaking of net ton miles per mile of road per annum?

A. Throughout, yes.

Q. Now, I understand you have also a map showing the freight traffic density of the Canadian Pacific expressed in gross tons miles per mile of track, this time, and not road?

A. Yes, Mr. Evans.

Q. That will be Exhibit 191.

...EXHIBIT 191..filed by Mr. Evans	:	Canadian Pacific Railway Company Freight Traffic Density Chart, Year 1948.

Q. (Cont.) That is a map, my lord, with various coloured lines entitled "Canadian Pacific Railway Company Freight Traffic Density Chart, Year 1948".

Now, that, I understand, Mr. Liddy, corresponds with a similar map, shown in Exhibit A in the Canadian National Submission?

A. Yes, sir, on page 70 of the Canadian National Submission.

Q. Now, would you explain to the Commission the basis of this map?

A. Freight traffic density on this Exhibit 191, is calculated on the basis of gross ton miles in freight service per mile of track for the year 1948.

Q. Now then, in order to get this distinction clear, the previous Exbibit was an indication of the density expressed in terms of net ton miles per mile of road and this Exhibit, as I understand you, is an expression of density in terms of gross ton miles per mile of road?

A. That is correct.

Q. Now then, would you go ahead and explain the basis of this map? First, you might tell us what a gross ton mile is?

A. A gross ton mile is a movement in road service of one ton including the weight of the car and contents over a distance of one mile.

Q. And what was the amount of work expressed in gross ton miles done by the Canadian Pacific in 1948?

A. They aggregated 57½ billion gross ton miles.

Q. Now, I think we did discuss this morning the difference between miles of track and miles of road and perhaps we need not mention that again, but how was the

freight traffic density as shown on this map calculated?

A. it has been calculated by dividing the gross ton milss in freight service for the year 1948, by the miles of track.

Q. Now then, how is that density indicated on the map which is Exhibit 191?

A. There are three categories, Mr. Evans. The first category is indicated in green and represents density in excess of 1½ million gross ton miles per mile of track per annum.

Q. And the second category is the one in yellow, I gather?

A. Yes, and that is density between 1½ million and 250 thousand gross ton miles per mile of track per annum.

Q. And the red is below the figure of 250 thousand gross ton miles per mile of track per annum?

A. That is correct.

Q. And that is all shown in a little table in the lower right hand corner of Exhibit 191?

A. Yes.

COMMISSIONER INNIS: Can you explain, Mr. Liddy, the fact that there are certain short stretches of line, from Empress to Swift Current, where there seems to be a very heavy traffic and in the east from Tring Junction to Sherbrooke? In the main this long haul traffic is where one gets this heavy density and one wonders what the explanation is?

A. I think a traffic man would know more about that than I do, but I would say that some of the traffic going from Tring Junction to Sherbrooke perhaps represents the haulage of asbestos and the activity connected with that

development.

Q. Perhaps there is some local explanation?

A. I would think so, sir.

MR. EVANS: What was the other one, sir?

COMMISSIONER INNIS: Empress in the west to Swift Current.

MR. EVANS: You might get some explanation of that by looking at what the direction of the flow of traffic is. The flow of traffic might indicate that it is traffic originating on the line, and if it were, it is probably wheat.

MR. FRAWLEY: The strange thing is, from Empress to Bassano, for the main line, it is yellow. That is on the Swift Current - Bassano line, and it seems strange that at Empress it passes from green to yellow.

MR. EVANS: Which do you say passes from green to yellow?

MR. FRAWLEY: When you are proceeding from Swift Current to Empress, and then after you pass Empress going on to Bassano it goes into the yellow class.

MR. EVANS: I am sorry that Mr. Liddy is not a traffic man, but I venture to suggest to you that the preponderance of traffic moves eastward from Empress, and they would not back-haul it, but would take it down the line from Empress, and I suppose the accumulation of traffic shows a heavier density on that line.

MR. FRAWLEY: Your other map shows 6.2 from Rosemary to Empress and 7.2 from Leader to Wickett - I don't know - eastbound; it is all eastbound.

(Page 16791 follows)

MR EVANS: You found it on the other map, did you?

MR O'DONNELL: Right on the boundary line, the Saskatchewan and Alberta boundary line.

THE WITNESS: I think the explanation, Mr. Evans, lies in the fact that these two lines are border situations; one is just below---

MR EVANS: Q. Just below the green, and the other is just over the green?

A. That is right.

MR FRAWLEY: There should be an extra colour there.

MR EVANS: Yes; we don't want any mysteries, though, Mr. Frawley.

Q. Now, I gather that the table on the lower right-hand corner also gives the mileages in each category, and perhaps you would indicate those, Mr. Liddy?

A. In the first category, that is, the heavy---

Q. The green?

A. The green category.

Q. A million and a half gross ton miles per mile of track per annum?

A. There were 8,600 miles; that is 47 per cent of the system. And in the yellow category, that is, between a million and a half and 250,000 gross ton miles per mile of track per annum, there were 5,400 miles of track, 29 per cent. And in the third category, that is, the red designation, there were 4,400 miles of track, or 24 per cent.

COMMISSIONER INNIS: What were the corresponding figures in the Duff Commission? Have you got those?

MR EVANS: Well, the Duff Commission used the net ton miles per mile of road. It is very difficult to

make them comparable. We tried to make this comparable with the map put in by the Canadian National, so the Commission would be able to make the comparison.

Q. Now, I notice that the Canadian National brief makes some reference to the lower category as unprofitable; have we made any study or have you made any study of the Canadian Pacific lines to determine whether any one or other of the categories can be considered unprofitable?

A. No, we have not made a study. We have simply adopted the same categories as the Canadian National.

COMMISSIONER INNIS: One could assume, I suppose, that the yellow and the green are always profitable and the red dubious?

MR EVANS: Well, we think all our lines are unprofitable today, taken together, but where the border line comes I think is impossible to say without a study; I would think so.

Q. Perhaps you would like to comment on that question of Dr. Innis', Mr. Liddy?

A. Well, I do not think there are any two lines exactly the same, but with the operating ratio as high as it is today, only five cents retained out of a dollar, it would seem that you have to search far and wide for a profitable line.

COMMISSIONER INNIS: Q. Still, the five cents might be made up say of fairly reasonable returns on green lines, the long haul lines, and perhaps substantial loss on the short red and yellow lines; but you have no way of telling that?

A. We have not made any study. I do notice on this map that there are a lot of red lines in the prairie provinces, which is Crows Nest territory; that is, not only is it low traffic density, but it is also low rate

per ton per mile territory.

MR EVANS: Q. Now, Mr. Liddy, I want to turn to another subject. Mr. Moffat, who was the witness for Manitoba, in his evidence at page 8695 made a statement regarding the cost of moving traffic; I would like to read it to you and ask you your views. It is about the middle of the page:

> "We obviously do not have the necessary data to make such an analysis, but there does seem to be evidence that terminal costs (a) above)" --

he has been discussing something in his brief --

> "have probably increased more sharply than line haul costs (b) above)."

Now, have you considered the matter of the increase in terminal costs as compared with the increase in line haul costs, and if so would you like to make some comments?

A. Yes; I have prepared a statement showing an analysis I have made over a period of twenty-five years. I would like to file this as an exhibit.

MR EVANS: That will be Exhibit 192. It is entitled "Canadian Pacific Railway Company. Analysis of Transportation Expenses showing ratios of accounts 373 and 376 to 391 inclusive and of the balance of accounts to total transportation expenses - rail years 1924-48."

---EXHIBIT 192: C.P.R.Co. Analysis of Transportation Expenses showing ratios of accounts 373 and 376 to 391 inclusive and of the balance of accounts to total transportation expenses - rail years 1924-48.

MR EVANS: Q. Now, would you explain the basis of that analysis, Mr. Liddy?

A. In this exhibit 192 the transportation expenses for a period of twenty-five years from 1924 to 1948 have been segregated between the primary accounts, which are

predominantly terminal costs---

Q. Such as?

A. Such as the cost of operating yards and stations, and the balance of the accounts, which largely pertain to the cost of moving the traffic over the line.

Q. Why did you restrict your study to transportation expenses?

A. Because, Mr. Evans, they are more directly related to the actual movement of traffic, and also because they can be allocated more easily to terminal and line haul operations than the other operating expenses.

Q. Now, in making this analysis what, if any, evidence have you found to support Mr. Moffat's suggestion that terminal costs have probably increased more sharply than line haul costs?

A. I found no evidence supporting Mr. Moffat's suggestion. As can be seen from the statement, the ratio of terminal costs to total transportation expenses increased slightly during the period 1924 to 1931, but it remained practically constant in the next ten years. During the war the ratio declined gradually, and for the year 1948 was almost identical with the average for the entire 25-year period.

Q. That is to say, you have got the average in the bottom line, showing that the ratio of transportation accounts is 32.41 -- that is, the ratio of transportation accounts 373 and 376 to 391 inclusive is 32.41 -- and in 1948 the ratio for the year was 32.5?

A. Yes.

Q. Now, what conclusion would you say could be drawn from that analysis?

A. From the results of this analysis the fluctuations in terminal costs and line haul costs appear to have been

very much the same over the period under study.

MR EVANS: That concludes the examination in chief.

THE CHAIRMAN: Mr. Brazier.

CROSS-EXAMINED BY MR BRAZIER:

Q. Have you Part I, Mr. Liddy, of the C.P.R. brief there?

A. Yes, Mr. Brazier.

Q. At the beginning of your examination yesterday you read into the record a part from page 60 of Part I; I believe you started at the sentence:

> "It may seem to the superficial observer simple to ascertain what is the actual cost of service. In fact, however, the problem of disentangling joint costs is one of great magnitude....."

Now, just stopping there, Mr. Liddy, would you tell me what kind of costs you are referring to when you use the term "joint costs" in that sentence?

A. I am using it in a rather broad sense, Mr. Brazier; primarily, though, freight and passenger to begin with, and after that joint costs common to various classes of traffic, freight traffic.

Q. Do you recognize a distinction between joint costs and common costs?

A. Well, it must be very fine.

Q. I would like to quote to you---

THE CHAIRMAN: Pardon me a moment. You said joint costs and what?

MR BRAZIER: Common costs.

Q. I would like to quote to you and see whether you would agree with a distinction given by Professor Healy in his book, "The Economics of Transportation in America." I

will just read one paragraph here and ask you if you---

A. What period of time was that book issued, Mr. Brazier?

Q. I think it is about 1940 sometime, Mr. Liddy -- yes, 1940.

A. Thank you.

Q. Reading from page 161, the last paragraph on the page:

> "It should be noted in this connection that such items as maintenance-of-way expenses are not joint costs, according to the common usage of that word by economists which implies that the joint nature of the costs has certain effects on pricing. The strict interpretation of joint costs is commonly illustrated by the example of the production of cotton and cotton seed, in that one cannot be produced without the other. On a railroad, track can be maintained for freight trains without necessitating the running of passenger trains, thus making track maintenance a common cost but not a joint one. The principal instance of true joint cost in the railroad field comes from the empty return movement of cars. There is no way known whereby cars, trains, and crews can be moved in the direction of traffic without being moved back again regardless of the traffic needs in the reverse direction."

Would you agree with that distinction as to the two types of costs?

A. I see nothing wrong with that. He has defined joint costs, and then he goes on to say what they are.

Q. What I want to see is if you are not actually on page 60 referring to what he terms common costs rather than joint costs?

A. No, I think I was referring pretty broadly to these costs that are entangled, whether they are joint or whether they are common. I am just looking at it as a practical railroader.

Q. But the greater part of this would be common costs as he defines them rather than joint costs as defined by Professor Healy; is that correct?

A. Well, I would have to make a study of Healy before I could really give you an intelligent Yes or No answer to that.

Q. Have you ever heard of that distinction before, Mr. Liddy?

A. No, I -- I have heard of it, but in our work---

Q. You never paid any attention?

A. In our work we like to be a little more down to the earth.

Q. You do not think that is being down to earth, to make a very vital distinction such as Professor Healy makes there?

A. You ought to talk to some of our operating officers.

Q. Mr. Liddy, I would like to ask you a few questions in regard to Exhibit 180, which you filed. Have you the exhibits in the 21% Case with you? I want to refer you back to the exhibits filed.

A. I find we have not got them just here.

Q. Well, probably between us we can use the copies that I have here.

A. This is going to be a common or a joint effort here?

Q. This will be a common effort, I hope. Now, Exhibit 180, you state in your evidence, was prepared in accordance with Exhibit 138 filed in the 21% Case?

A. Yes.

Q. Which gave the similar information for the years 1936, 1937, 1938, 1939, 1940, 1944, 1945 and 1946?

A. Yes.

Q. Now, the same information, the same breakdown for the year 1945, was also set out in an earlier exhibit, being Exhibit No.28; is that correct? That corresponds to---

A. Well, there is a slight difference, Mr. Brazier, between these two exhibits. One is based on operating revenues and operating expenses and the other is based on gross earnings and working expenses. Outside of that, I believe that they are---

Q. These two are different for this year?

A. Yes. If you notice, Exhibit 28 is captioned "Apportionment of gross earnings and working expenses including taxes", whereas Exhibit 138, which is the basis that I used in preparing Exhibit 180, speaks of railway operating revenues and railway operating expenses, and does not, of course, take into account taxes, hire of equipment and joint facility rents and so forth.

Q. With that distinction, Mr. Liddy, those exhibits are the same, and were drawn up for the same purpose?

A. I believe they were, Mr. Brazier.

Q. What I want to call your attention to, Mr. Liddy, is the fact that it is on Exhibit No.28 that you set forth the explanation of the method used by yourself in allocating various expenses as between passenger and freight; is that correct?

A. For the purpose of---

Q. That is, I refer to Exhibit 28 in the 21% Case.

A. Yes, we were asked, Mr. Brazier, to file these figures upon, I believe, request of the Board, or maybe---

Q. I think probably at our request on that one, that first one.

A. I see.

(Page 16802 follows)

Exhibit No. 138 in the 21 per cent case was filed at the request of the Board.

A. I have forgotten, you are probably right.

Q. And this exhibit sets forth the various bases upon which allocations are made, in dividing your revenue and expenses, or your expenses as between freight and passenger service.

A. That is the basis of the formula we follow.

Q. I suggest to you that you use many different bases, depending upon the item which you are allocating. Do you want to look at the following?

A. Oh, yes. There would be various -- using the primary accounts, we may use various bases.

Q. For instance, some were allocated on the basis of gross ton miles?

A. That would be probably track elements.

Q. Roadway maintenance, containing tunnels, and all that?

A. Yes.

Q. And then, maintenance of fuel and water stations; that was apportioned on the basis of tons of fuel consumed in the transportation service?

A. Yes.

Q. Taking locomotive repairs, depreciation and retirements were apportioned on the basis of tractive effort miles?

A. Freight and passenger.

Q. And the apportionment of traffic solicitation expenses, was made on the basis of an analysis of the duties of the staffs in the various traffic offices?

A. Yes. There was no statistical basis which seemed to apply in that case, so we made an analysis.

Q. And yard transportation expenses were apportioned on the basis of yard engine use?

A. Freight and passenger, yes, sir.

Q. And there were a great many other bases for different items?

A. Yes, bases which are readily available to railway officers.

Q. Yes, and which are generally accepted by them as being a good measure of allocation?

A. Yes. Some of them are pretty fair. None of them are precise.

Q. No allocation could be, I presume.

A. It is very difficult, unless you have as many accountants as you had operating men, keeping the exact time.

Q. Is that the situation which exists in the United States?

A. The situation which -- no, I do not say so.

Q. They make those allocations in their primary accounts?

A. Not quite that way.

Q. Not quite that way?

A. No.

Q. You have not used the I.C.C. bases for them?

A. We have the advantage of knowing what the I.C.C. basis is. As a matter of fact we do apply the I.C.C.basis in some small parts of our system. We are quite acquainted with the I.C C. basis.

Q. Going on to Exhibit 180, it shows that only 32 per cent of your railway operating expenses are directly severable in the company's accounts. Is that correct?

A. Yes. That is the footnote to Exhibit 180.

Q. Would you say that because of that small percentage

which can be directly credited or charged against the two services, that the statement lacks significance?

A. What do you mean by "significance"?

Q. Would it be of any value to the management, for instance, to have that information before it?

A. Well, I have been with the company for many years, but I have never yet got them to sit down and look very seriously at a statement like this.

Perhaps if you had a different kind of manager -- these fellows are all practical men, and the first question they ask me is: How did you arrive at that figure? And then I will say, I apportioned it. Then they will say: On what basis? Then I will say: On an arbitrary basis, or according to some yardstick. Then they will" say to me: Oh!

What the management is concerned with -- and the figures are very clear on Exhibit 180 -- is: that for passenger service there were $62 million taken in. That is a known figure.

Now, we also know that we outlayed $39 million for direct expenses. That too is a known figure.

We are interested in those two figures, very much interested.

Now, in between the figure of $39 million and $62 million is a breadth of $23 million; and it is the view of our management that, passenger service having paid the $39 million, there is that $23 million left over for these common or joint expenses, and that they have done about all they can with passenger service, except to make sure that every dollar spent in passenger service is well spent, and that no dollars in passenger service are spent that could be avoided.

Q. Yes?

A. Everybody recognizes that one dollar of passenger revenue practically goes directly into net.

THE CHAIRMAN: Q. Goes where?

A. Directly into net. If you pick up one dollar passenger revenue, then your net is going to be influenced by an extra dollar. On the other hand, if you lose a dollar in passenger revenue, then your net goes down a dollar. They are interested, as practical men, in this problem of freight and passenger.

MR. BRAZIER: Q. You are not suggesting, I presume, that the $39 million represents full out-of-pocket costs of the passenger service?

A. No.

Q. It would be something over that figure, at the very minimum, would it not?

A. That is right.

Q. And if the figure for 1948 -- if the business done in 1948 maintained a figure of $23 million, I presume you would say that is a satisfactory difference?

A. No. I do not say they would be satisfied with it.

Q. Would they be concerned with it if that was the only difference they had?

A. They are not concerned in the way that you speak of.

Q. Let me put it this way: supposing in 1949 the difference between those two figures was only $10 million. If management did not have that figure before it, it would not know the true situation at all, would it?

A. Well, I can assure you that every operating officer in the Canadian Pacific knows this situation: that passenger service is not remunerative to the extent of freight.

Everybody knows in the Canadian Pacific -- every operating officer, whether he has Exhibit 180 or

not in front of him knows that every dollar which can be saved in passenger service is a saving that should be made; and when we come, as a practical problem, to what you are going to do with passenger service -- first of all, you have got to pick out a train. That is the first question the operating officers ask: what train will we cut off?

Before we can cut off a train, we have to go before the Board. You know the procedure.

Q. I want to find out just how far management follows this matter up.

THE CHAIRMAN: Q. You say that if you wish to cut off a train, you must first go before the Board. Do you refer to your board of directors?

A. No; the Board of Transport Commissioners.

Q. To cut off a train?

A. Yes, if we are going to curtail a service.

Q. You must keep a service going as it is until you have first obtained the permission of the Board?

A. Yes, that is right. And also, with respect to branch lines. If you want to curtail the service on a branch line -- we have innumerable branch lines where we have to provide tri-weekly or bi-weekly passenger service, and where you will find just a spattering of passengers.

Everybody knows that those trains do not pay. So what are you going to do about it? You can save money if some person will let you cut a train off; and it would be in the national interests to so curtail your service.

Q. You say in the national interest to do what?

A. To curtail that service.

Q. To curtail it?

A. Yes, sir.

Q. Suppressing it entirely is one thing, and abandoning it is another?

21 per cent case in front of you?

A. Yes.

Q. That indicates that the total passenger revenue in that year was, roughly, $84 million? Is that correct?

THE CHAIRMAN: What year was that?

MR. BRAZIER: Q. 1945.

A. Yes. $83,945,000.

Q. Yes. And in 1948 that revenue had dropped to $62,617,000 odd?

A. 1948?

Q. That is Exhibit 180?

A. Yes.

Q. Roughly, your passenger revenue between those three years has dropped approximately by something over $20 million?

A. Yes.

Q. I also call your attention to the fact that in 1945 the expenses solely related to the passenger service were $33,803,000 odd?

A. Yes.

Q. And those expenses, solely related, in the year 1948 had increased to $39,175,356?

A. That is right.

Q. That is an increase. While you have a revenue decrease of over $20 million, your expenses which are directly severable have increased by $6 million?

A. Yes. But you will understand that the year 1945 was the year when we were carrying home the troops, and people were sleeping in upper berths.

But in the year 1948 they are not sleeping in upper berths, and wages and material prices have greatly increased.

Q. I would like to make this suggestion to you to

see if you would agree with me that the greater part of the difficulty which the railways have been suffering in the last year or so is due to your decline in passenger traffic, and the tremendous loss that the railways incur as a result of that decline?

A. I really thought my difficulty was in getting reasonable freight rates.

Q. You do not agree with that?

A. No, sir.

Q. Now, the Canadian Pacific Railway operates lines in the United States?

A. Short lines.

Q. And for those lines you have to file reports with the Interstate Commerce Commission?

A. That is right.

Q. And in those reports which you file with the Interstate Commerce Commission, you have to break it down as between freight and passenger traffic?

A. Just the same as all the other class 1 railways do in the United States.

Q. In the report that you filed for the year 1948, can you tell me what percentage of the expenses of the passenger service you were able to allocate definitely to the passenger service?

A. No. I could not tell you that. I would have to look at the report.

Probably the answer you would like to get is: that on United States railways the proportion of expenses which are directly allocable is larger than 32 per cent.

THE CHAIRMAN: Q. Larger than what?

A. Larger than 32 per cent.

MR. BRAZIER: Q. How much larger?

A. I have forgotten. It might be 40, 50 or 60 per cent.

Q. I suggest to you that it is over 60 per cent?

A. I will accept your figure.

Q. You will accept it?

A. Yes, but subject to check.

THE CHAIRMAN: Q. We can see the figures, can we not?

A. Oh, yes, we could look it up. I have not got any of these reports with me. But whatever figure the Canadian Pacific might have, let us say, on its line in Maine, would be of no significance. It might be 15 per cent or it might be 90 per cent.

MR. BRAZIER: Q. I suggest to you that if in Exhibit 180, 60 per cent of the expenses had been solely related to the passenger traffic, it would have given you -- the expenses solely related to the passenger traffic, without any allocation, an apportionment of something over $70 million?

A. Would you give the derivation of those figures?

Q. You have got 32 per cent. That is $39 million. Now, if you take 60 per cent instead of 32 per cent --

A. I would still like to see your mathematics.

Q. I am not trying to be accurate or anything, to the dollar.

A. My difficulty -- perhaps I have not understood your question -- is: supposing the expenses were 100 per cent allocable; you might have more expenses than I have shown here.

Q. You have got a certain amount of expenses there, being a total of $91 million odd for passenger, and $234 million odd for freight service. That is the total expenses?

A. That is right.

Q. And I say that if 60 per cent of that total was

directly allocated to passenger and to freight rather than the 32 per cent --

A. There is no relationship between those two figures at all. If you put those figures down on a piece of paper you will satisfy yourself that there is absolutely no relationship between them. The 32 per cent represents the amount of expenses that could be segregated. You might have 100 per cent.

Q. Yes?

A. And you would not change the figures at all.

Q. But that is not a likely situation, is it? Because if you are directly allocating 60 per cent of your expenses, you are going to have a lot more than $39 million.

A. Yes, and a lot less of the fifty-two.

Q. That is right. And I suggest that if you did it on that basis, the $39 million would turn into almost $70 million, if not a lot more?

A. I do not know.

Q. Well, if that is correct, then the passenger service would show a very definite loss of $8 million.

(Page 16816 follows)

Q. Well, if that is correct then, the passenger service would show a very definite loss of $8 million?

MR. EVANS: No.

MR. BRAZIER: I am saying assuming my proposition is correct.

THE WITNESS: I believe that the passenger service today, that is for the year 1948, has not been a burden on freight in total.

THE CHAIRMAN: Has not been a burden - - ?

A. On freight in total. It has not contributed very much to this joint or common expense, but it has not been a burden; it has paid all its direct expenses. It has paid something towards the salaries of our operating officers, something towards maintenance, and, in my view, it has not been a burden.

MR. BRAZIER: You are familiar with the rules governing the separation of operating expenses published by the Interstate Commerce Commission?

A. I have seen them yes.

Q. Now, Mr. Liddy, you would be willing to agree, I presume, that the Santa Fe Railway in the United States is one of the best-managed railroads in that country, one of the most successful railroads?

A. I would think so. I do not know anything about that railway, but I would say it was a well-managed road.

THE CHAIRMAN: Is that the railway's reputation?

A. Well, the only thing I know about it, is they have got a good song about it.

MR. BRAZIER: Well, in the 21 Per cent Case your Company drew certain comparisons between the Canadian Pacific Railway and the Santa Fe Company and held the Santa Fe up

as one of the examples of a well-managed railroad.

A. Well, they may have; myself, I did not draw any comparisons.

Q. Have you ever made a study of the accounting rules published by the Santa Fe Railroad?

A. No.

Q. Are you aware of the fact, that that railway goes even further than required by the Interstate Commerce Commission in segregating its passenger and freight costs?

A. I don't know anything about it.

Q. Mr. Chairman, I have obtained, and unfortunately I have only the one copy, but I would like to file it with the Commission for the use of the staff, and it is entitled "Santa Fe - Accounting Department, Instructions Relating to the Distribution of Operating Expenses, Taxes, Equipment Rent and Joint Facilities. Rents" and this is the important part as far as I am concerned, that while the Interstate Commerce Commission makes that division on a system basis between freight and passenger, the Santa Fe Railway has seen fit to make the same division between operating districts and also as between various states which the Railway passes through.

THE WITNESS: I think they are required to do that in any event, Mr. Brazier.

Q. Well, the Commission has the other rules before them and they can make a comparison of it.

A. The Interstate Commerce Commission rules require you to break down your expenses, freight and passenger, to the smallest operating division that you can get.

...EXHIBIT 193..filed by Mr.Brazier : Santa Fe - Accounting Department, Instructions Relating to the Distribution of Operating Expenses, Taxes, Equipment Rent & Joint Facilities Rents.

COMMISSIONER INNIS: Have you any further information about the Santa Fe, Mr. Brazier?

MR. BRAZIER: No, just what is contained in that.

COMMISSIONER INNIS: You have not any information as to what they actually do allocate to passenger?

MR. BRAZIER: It is all set forth in that, and it is done on the published basis for different primary accounts.

COMMISSIONER INNIS: For different years?

MR. BRAZIER: No, that is a standard.

COMMISSIONER INNIS: What I wanted to find out was whether in any year you had any indication as to what the percentage was in the Santa Fe as a result of this?

MR. BRAZIER: I think I could probably obtain that from the Interstate Commerce Commission Reports. I will check to see if that is available. I am not quite sure.

COMMISSIONER INNIS: I am wondering if they go any further than the Interstate Commerce Commission if it would throw any light.

THE CHAIRMAN: What did the Santa Fe succeed in doing according to this?

MR. BRAZIER: This is the Instruction Manual which is published to their Accounting Officers advising them as to the breakdown of the expenses that they are to make.

THE WITNESS: May I see a copy of that Exhibit, Mr. Brazier, for a minute?

MR. BRAZIER: Yes, certainly.

MR. O'DONNELL: Have you got a copy for us, Mr. Brazier?

MR. BRAZIER: No, I have only the one.

THE CHAIRMAN: Well then, I think this would be a

good time to adjourn.

...RECESS

...UPON RESUMING

THE WITNESS: During the Recess, Mr. Brazier, I have looked at this Exhibit 193, and in case you have overlooked it, may I say that this is instructions to the Santa Fe Accounting Department, and it reads:-

> "To conform to Interstate Commerce Commission rules governing the separation of operating expenses etc. between freight service and passenger service."

and I think if you read the details, you will find that this is merely instructions carrying out the I.C.C. rules and instructing the employees of the Santa Fe to divide these expenses between states.

MR. BRAZIER: And operating districts?

A. Between states particularly for the purpose of other reports to regulatory bodies.

THE CHAIRMAN: Does it not deal with the separation between passenger and freight?

A. Oh, yes, this simply says: "To conform to the I.C.C. rules. They instruct all railways in the United States to do that.

Q. You said something about "between states"?

A. Yes, that is the Santa Fe system operates over probably five or si: states and in each state public authority requires an annual report.

Q. An annual report on all these things - passenger and freight, for instance?

A. Very similar to the Canadian Pacific Report we

make to our Dominion Bureau of Statistics. It requires not only one report, but the Interstate Commerce Commission requires a report for the entire system and each individual state through which that railway runs requires a report of the traffic and other statistics pertaining to that state.

Q. And divided up between passenger and freight traffic?

A. Yes, sir, very burdensome regulations.

MR. BRAZIER: There is no Interstate Commerce Commission requirement as to the State apportionment?

A. No.

Q. And as far as you know there is no State requirement as to the operating district apportionment, is there?

A. Well, that would be naturally kept. The Interstate Commerce Commission's rules say that you shall keep these expenses by the smallest unit of operating division. That is the essence of the Interstate Commerce Commission's rules, and therein lies its burden.

Q. Now, Mr. Liddy, I want to refer you to a statement in Part I of the Canadian Pacific Railway's Brief at page 124, the first full paragraph on that page, which reads:-

> "In the era when passenger traffic was the exclusive preserve of the railways, knowledge of the cost of this service was of value and of significance in rate cases. Since then, air and highway transportation have grown to such an extent that it is out of the question to establish passenger rates in relation to cost of service and a separation of expenses between freight and passenger has lost much of its former significance. From management's point of view, a passenger service' 'income account', in effect, would be of

no more than academic interest in face of the hard fact that the railways are under obligation to continue supplying passenger service".

Now, I wanted to ask you why you think that knowledge of this subject was more important in rate cases when you had a profitable service than it is today?

A. Well, I thought that was elementary, Mr. Brazier. If in, say, the period 1910, 1912, your passenger services began to show a loss - -

Q. That early? I suggest it was around 1920 and 1921.

MR. SINCLAIR: Let him finish, Mr. Brazier . He said "if". I think you should let the witness finish.

THE WITNESS: Then we would, in such a circumstance, have a good case to go before the Board and say: "The passenger rates should be increased; we are not making enough net", and if that was the view of our passenger people, that passenger service would stand an increase, that is what is meant in this Brief by the words "...would have significance in rate cases". But the situation now, is that even if we are operating at a loss, even granted that we are operating at a loss, what are you going to do about passenger rates - drive it over to the buses and airplanes?

THE CHAIRMAN: One point that occurs to me out of the first sentence of the paragraph, is that apparently in the older days you had a knowledge of the cost of service and said it was of value. You must have had some means of arriving at it?

A. We have today, sir.

Q. The same means as today?

A. Yes, sir.

Q. That is, some are identifiable costs and the rest

are apportioned?

A. Yes, sir. No two people have exactly the same views.

Q. I thought perhaps you had a better system of accounting in the old days, but it is the same as now. I mean, certain expenses were earmarked exclusively to passenger service, and as to the rest, you could not earmark in that way and you apportioned it?

A. Yes, sir.

Q. You always did that, and never did anything else?

A. That has always been operating in our accounts.

Q. I mean, when, as you say, these figures "...were of significance in rate cases", that is what you say here?

A. Yes.

Q. This is the same sort of information which you supply now?

A. The Interstate Commerce Commission, Mr. Chairman - -

Q. We are talking here about Canadian rate cases.

A. We have had this information for years and years, and in the United States the Interstate Commerce Commission started to divide freight and passenger as early as 1888.

Q. But I am not interested just now in that. I mean to say, that when you say here in your Brief that formerly when you had, we might say, a practical monopoly of passenger service, the knowledge of the cost of that service was of value to you and was significant in you r rate Cases?

A. Yes.

Q. I thought perhaps you just meant that in those days you employed better means of allocating more exactly the cost of passenger service than you can do today, but you tell me No, it is the same way?

A. No, that was not the thought.

MR. BRAZIER: Can I presume then, Mr. Liddy, that in the old days that you were speaking of, that the company would have been fully justified in going before the regulatory body with cases similar to that which you have on Exhibit 180 and asking for an increase in passenger rates?

A. Well, that would have been one of the factors. No doubt there would be increased wages, increased material prices, the same as we have had in these recent freight rate cases - other factors.

Q. Now, have you anything more to say on that?

A. No.

Q. I just want to ask you some questions, Mr. Liddy, about the Other Income Account?

THE CHAIRMAN: Are you referring to an Exhibit?

MR. BRAZIER: Just some general questions first, Mr. Chairman. Mr. Liddy, do you know when the other Income Account was established as such?

A. I would not be surprised it might be the same year as we show in our digest of development, page 27 in the Appendix to Part I. It would be around the year 1892, I take it.

Q. Mr. Liddy, I have before me some of the Annual Reports of the Canadian Pacific Railway and I find this statement in the Annual Report for the year 1911. It is found at page 9 of the Report of that year, paragraph 14, and reads:

"You will have observed that in this Annual Report earnings and expenses of your railway and steamship lines are shown together, and that the revenue from other sourses is given

in a separate statement. This is in accordance with the policy outlined by your directors in the circular letter of March 15 last".

Now, I suggest to you that that is when the Other Income Account was established.

COMMISSIONER INNIS: What page was that account?

MR. BRAZIER: That is in the Annual Report for the year 1911.

THE WITNESS: Well, I don't know as to that, Mr. Brazier.

Q. Have you examined the early Annual Reports of the Company?

A. No, I have never gone back very much into those Reports. I would not be surprised but that these figures may be taken from the Reports that were made to the Dominion Government.

Q. I would suggest to you that the figures on Exhibit 190, prior to the year 1911 are actually your steamship earnings which have been taken out of your General Report of that year and shown separately on this Exhibit?

A. You may be right.

THE CHAIRMAN: Of what particular year?

MR. BRAZIER: Prior to the year 1911.

THE CHAIRMAN: The entries there begin with the year 1892?

MR. BRAZIER: Yes, from 1892.

THE CHAIRMAN: And are you saying now, that down to the year 1911 you think these represent only steamship income?

MR. BRAZIER: Yes, which were before that time not even treated separately in the Annual Reports, but

which have been taken out for the purpose of this Exhibit 190 showing them separately. I will just show you these two Annual Reports, Mr. Liddy. There is the Annual Report for 1910.

COMMISSIONER INNIS: What are the steamship earnings for that year?

MR. BRAAZIER: It says "Net earnings of steamships in excess of amount included in Monthly Reports $909,235.

THE WITNESS: I would really have to look at our detailed Report to the Dominion Government before I could say anything specific about this.

Q. I will show you the Annual report for 1911, where, for the first time, they give "The following are the details of Other Income for the year ended June 30, 1911".

A. Well, that might have been the way we reported to the shareholders.

THE CHAIRMAN: And that includes things besides the steamships?

MR. BRAZIER: Yes, it includes many things - interest on cash proceeds and all bank payments for land, interest on deposits and loans, interest from a number of railway bonds, interest from Dominion Government bonds, interest from Ontario Government bonds, interest from British Consuls - -

THE CHAIRMAN: Well, all those things must have been accounted for in some manner previously?

(Page 16827 follows.)

MR BRAZIER: But in the Annual Report they were all in the one account.

Q. I would also call your attention, Mr. Liddy, to a statement contained in the Report of the Proceedings of the 32nd Annual Meeting of the Shareholders, held on October 1, 1913, which statement is found at page 6 and reads as follows:

> "The railway companies in the United States are required to segregate their railway earnings proper and their income from other sources, and, while there is as yet no similar legal requirement in Canada, we have, as you know, recently made such a change in our system of accounting as to practically conform to the practice of other railway companies, but we still include in the earnings of the railway returns from our commercial telegraphs system and our Pacific Coast steamships. In the next Annual Report the revenue from these sources will be treated as special income, and of course there will be a corresponding reduction in the gross and net earnings of the railway."

And one further section, Mr. Liddy, in the Annual Report of the year 1914, found at page 11 of that Report, paragraph 18:

> "The net revenue of the commercial telegraph system, Pacific Coast steamers and News Department, that in previous years had been incorporated in the revenue of the railway, is deducted from the surplus shown in the revenue statement this year and transferred to special income accounts."

Now, I suggest to you that those sections deal with the beginning of the account now known as Other Income?

A. They no doubt are true records.

COMMISSIONER INNIS: You have no suggestion as to why this was done, Mr. Brazier?

MR BRAZIER: No. I thought it might be enlightening if the company could make available to the Commission the circular letter which they refer to in the 1911 report. They say there, in setting the account up :

> "This is in accordance with the policy outlined by your directors in the circular letter of March 15th last",

which would be March 15th of 1911. Apparently the reason for setting up this account would be set forth in that circular.

Q. Do you know whether or not that would be available at this date, Mr. Liddy?

A. No, I wouldn't know. I have never seen it myself. I could make enquiries if you want me to. But what happened in 1915, 1914, 1913, is quite a long way now, Mr. Brazier, from where we are.

Q. I appreciate that, Mr. Liddy, but it might give us some light on why the Other Income account was set up?

A. Well, I think you will find the real reason is that around that time we got into freight rate cases, and we had to get down to the railway business. I think the first large freight rate case was the 1914 Western Rates Case. These gentlemen like Mr. Frawley know more about that past history than I do.

MR FRAWLEY: I thought there was a pretty important one in 1906-07.

THE WITNESS: What was the name of that one, Mr. Frawley?

MR FRAWLEY: The one that set up your Schedule A.

MR SINCLAIR: International rates.

MR FRAWLEY: International rates.

THE WITNESS: I do not think that had anything to do with revenue case, though.

MR BRAZIER: Q. Mr. Liddy, referring to some of the items included in Exhibit 189, which is the earnings on investments in enterprises which have been suggested from time to time should be included in the railway account, I just want to ask you one or two general questions about that. I think your remark was that so far as the Toronto Terminals Railway Company was concerned it was just another investment which you had made, and it could just as well have been in Dominion of Canada bonds, and then there would be no question as to it being Other Income. Do I correctly state the purport of your---

A. Oh, I think generally that is the case.

Q. Let us presume, then, you put that money into Dominion of Canada bonds; what would you have done for terminal facilities in Toronto?

A. Well, the Toronto Terminals Railway Company would have had to sell its securities on the open market, and I hope it could have got a price, an interest rate, that was close to five per cent. I doubt it; I doubt it. It would have to sell some of it in stock; I do not think it could sell bonds for its entire property investment.

Q. Not only do you own half the bonds issued by that company; you also own half the common stock, don't you?

A. Yes.

Q. And probably you would have had to guarantee the bonds issued by your subsidiary?

A. Well, we have had experiences with guarantees; they cost money.

Q. You are not seriously suggesting that your investment in that terminal company is the same as an investment

being made in Dominion of Canada bonds, are you, Mr. Liddy?

A. No; I do not think I said that.

Q. That is an investment made solely for rail purposes?

A. That is not the point, Mr. Brazier, at all.

Q. You think there is a distinction that can be made there?

A. Well, the Toronto Terminals Railway Company was set up by the old Grand Trunk Railway and the Canadian Pacific for the purposes of having a joint terminal, that is, saving the old Grand Trunk and saving the Canadian Pacific some investment in operating a station that was joint. Now, in order that these facilities might be built, the parent companies advanced the money to these two companies -- to this company, the Toronto Terminals Railway Company -- for its property.

Q. You think there is a distinction in handling it that way than if you built your own terminal in Toronto; it might cost you more, I will admit that.

A. Well, if we were to build say a $15 million station in Toronto ourselves that might have required financing by the way of some common stock, some preference stock, some bonds; and you would find that then in our property investment. Now, the Toronto Terminals Railway Company, the investment in that property in Toronto, is not in that figure of a billion and one.

Q. I quite appreciate that, Mr. Liddy.

A. So that whichever way you do it, this is the way that all U. S. railways have done it. There are hundreds and hundreds of joint facilities down in the United States.

Q. Do they charge the bond interest against their Other Income?

A. Yes, exactly -- we follow the I.C.C. accounting.

Q. Could you give me any examples, Mr. Liddy? I have never been able to find any myself where they made a charge of this nature to their Other Income.

A. Well, I have to refer you to the I.C.C. classification.

Q. Could you show me in a report of any American railroad?

A. Do you want to be shown?

Q. I certainly do, because I have not been able to find an example where an investment---

A. Have you written them?

Q. ---of this type is charged to Other Income.

A. Have you enquired anywhere?

Q. Yes.

MR SINCLAIR: Where? Better get it on the record, where Mr. Brazier has enquired and what he asked them. Let us find out.

MR BRAZIER: Q. Can you give me, Mr. Liddy, or would you be able to within a few days if you haven't it immediately available---

MR SINCLAIR: There is not much use in his duplicating the work Mr. Brazier has already done, so if he would tell us the ones he has written to we would be saved that effort.

MR FRAWLEY: Who is cross-examining whom?

MR SINCLAIR: I am just trying to keep the record clear.

THE CHAIRMAN: What is it you are asking to have done, Mr. Brazier?

MR BRAZIER: Mr. Liddy has said that the American railroads handle a situation such as this in exactly the same way, that is, they charge the bond interest to their

Other Income.

THE CHAIRMAN: "A situation such as this" -- are you talking of the Toronto Terminals?

MR BRAZIER: The Toronto Terminals.

THE CHAIRMAN: That is, several roads get together and create a new company; is that what you mean?

MR BRAZIER: And build a terminal, and then charge the interest on the bonds issued by the terminal company against their Other Income rather than against their Rail Income.

THE WITNESS: Mr. Brazier, I think if you just simply think of it for a minute you would find the answer. Supposing we made the Canadian Pacific Annual Report read "Canadian Pacific Annual Report and one-half of the Toronto Terminals Railway Company" -- that is what we would have to do if we did not put this---

Q. Now, Mr. Liddy, isn't this correct---

A. Now, just let me finish, please; I had not quite finished. This is a separate company. We do not own it, and the Canadian National do not own it. We only have an interest in it, and they have their own employees, they buy their own materials, and they have their own payrolls, and simply a plain statement of the fact is a refutation of what you are suggesting.

MR BRAZIER: Q. All I am suggesting to you is that the interest which you receive from the Toronto Terminals Railway Company on the bonds which you hold in that company should properly be credited to your rail income rather than to your other income?

A. I do not agree with you.

Q. You do not agree with that at all?

A. What would you do with the investment?

Q. You would put that, I presume, in your rail invest-

ment.

A. We would have---

Q. Is this the correct situation, Mr. Liddy, that the Canadian Pacific Railway Company as a rail enterprise does pay to the Toronto Terminals Railway Company rent for the use of the Toronto terminal?

A. That is under agreement; and the Canadian National pay rent.

Q. And that is charged against your rail operation?

A. That is right.

Q. And that rent which the Toronto Terminals Railway receives from you and from the Canadian N tional equally---

A. That is right.

Q. ---is in turn used to pay you the interest on your bonds equally?

A. That is right; and there is no investment in the railway property for that terminal, and that is a common arrangement and strictly in accordance with the prescribed classification of accounts of the I.C.C.

Q. I suggest to you, Mr. Liddy, that that may be of importance if you establish freight rates on a rate of return basis, but when they are established in the present manner it makes a considerable difference to the income which your rail account shows?

A. Well, it is absolutely fundamentally wrong to merge two companies together. They are two separate companies, the Canadian Pacific and the Toronto Terminals Railway, and we could not merge them in our accounts.

Q. Mr. Liddy, I will just ask you a question or two regarding communications now. Can you tell me what part of your revenue in the communication department is received from the railway , for services rendered to the railway as against the revenue received from the commercial

users? Probably, Mr. Liddy, if you could obtain that information and put it on the record---

A. I have it right here, Mr. Brazier, I think, in a minute. For the year 1948 the Canadian Pacific were charged with the following amounts for communication services performed by our telegraph department: Under maintenance account 247, $2,041,000, and operation account 407, $1,624,000, a total charge against the railway of $3,666,000. Now, the total expenses of the Canadian Pacific communications department was $7,813,000 -- that is after deducting these items that I speak of -- so that is a total expense, including the railway, of $11,400,000, so that the telegraph service rendered the railway was about a third of the total activity of our communications department.

Q. Are those the only two railway accounts that are charged with expenses of the communication system?

A. That is right.

Q. Now, Mr. Liddy, I would like to just ask you one or two questions in regard to depreciation. I presume I am correct in taking from your evidence that you are in favour of the user system of depreciation?

A. You are right, sir.

Q. Could you tell me what a normal year of operation is with the Canadian Pacific Railway?

A. I do not determine normal exactly for depreciation purposes. I can determine averages. Normal is a changing concept.

Q. I suggest to you, Mr. Liddy, that unless you take what is to be a normal year when applying a user basis of depreciation, upon which you are to base freight rate levels, you are going to have a distorted picture?

A. You assert that as a fact?

Q. I am asking you if you agree with that statement?

A. Well, Mr. Brazier, you are getting down now to the matter of determination of a rate, whether the rate of depreciation is correct or not.

Q. No, if I may correct you, Mr. Liddy, I am not speaking of the rate at all. Say you have struck your rate; now, I suggest if you take a year of high traffic, where you have a high traffic level, and fix freight rates for the future in that particular year, you are going to have a very large, much larger dollar charge than you would if it was fixed in another year of low traffic?

A. Under the user method?

Q. Yes.

A. Just the reverse. It is the fixed line method that is rigid, it is the fixed straight line method that is going to give you distortions. The user method, Mr. Brazier, goes up and down with your traffic and assesses against each unit of traffic the same charge, year in and year out, in good years and poor years.

Q. Mr. Liddy, what I am putting is, if you take a year such as 1948, or 1947, which was a year of high traffic level -- is that correct?

A. I would agree with that.

Q. And as a result of that on the user basis you get a very high charge in dollars for depreciation?

A. When you say high charge, you mean per unit of traffic?

Q. In dollars.

A. Yes, in dollars. I won't say it is a very high charge. We get a charge for depreciation in dollars that is related to traffic.

Q. I will put it this way, that it is higher than would be a normal charge if it was taken over a period of

years?

A. In dollars?

Q. In dollars.

A. Yes, but no more abnormal than the traffic is in that year above previous years.

Q. I suggest to you that that distorts the freight level that is fixed as a result of that high dollar charge?

A. Well, I do not agree with you.

THE CHAIRMAN: What is your proposition that Mr. Liddy does not agree with?

MR BRAZIER: If freight rates are fixed in a year of high traffic level with the use of the user system of depreciation, you have a high dollar charge in that particular year which is reflected into the requirements of the railways. As a result a higher freight rate has to be fixed than if it was fixed in a normal year.

COMMISSIONER ANGUS: Is not the point between you that Mr. Liddy thinks that is offset and more than offset by the high income in a high traffic year?

MR BRAZIER: Yes, but my point, Dr. Angus, is that freight rates are set for a period of years, and that level is struck in the year of high traffic level, and the level of freight rates does not come down.

MR SINCLAIR: Oh, now, just a minute, Mr. Chairman! The Board remains seized of these proceedings, and if the railways are earning too much they can on their own motion initiate reductions, and have done so; and I think it is very wrong for my friend, and I am sure he did not mean to put it that way, that the freight rate levels do not come down. I mean, history has proven that they did.

MR BRAZIER: I will refer your lordship to a section later in the judgment in which that subject is

dealt with, in the last judgment of the Board of Transport Commissioners.

THE CHAIRMAN: The last one?

MR BRAZIER: Yes.

MR FRAWLEY: The second last one.

MR BRAZIER: In the 8% Case; it is dealt with in there.

Q. Now, Mr. Liddy, I think I have just---

A. I of course do not agree with that section of the judgment---

Q. What I have stated is in fact what the Board found in its judgment, isn't it?

A. I do not know what evidence they found that on. It is a statement---

Q. It is in the judgment, though?

A. Oh, yes, I will agree it is in the judgment. A lot of things in the judgment we don't agree with. Because it is in the judgment does not prove that it is right.

Q. Just one other question with regard to using the user system of depreciation. You use that in relation to fences?

THE CHAIRMAN: In relation to what?

MR BRAZIER: Fences; that is quite an item, I think, in the railway investment.

Q. You take---

A. The user basis for fences?

Q. Yes; it is in your depreciable road property?

A. Oh, yes. We allocate the loss of service value of all our property over years on the basis of units of use, irrespective of whether it is equipment---

THE CHAIRMAN: Q. That is, all your depreciable property?

A. Yes, irrespective---

Q. You include fences?

A. Fences is a depreciable item -- telegraph poles.

Q. That is, they are not on a renewal basis?

A. That is right; ties and rails, they are renewals.

Q. Yes, that is what I understood.

A. Stations and bridges and fences and signals.

MR BRAZIER: Q. I just want to take the one, fences, for illustration. That is depreciated upon a basis of so many gross ton miles of traffic?

(Page 16838 follows)

A. I did not segregate these individual items. We are on what we the group basis. You are thinking of some details of the I.C.C. Bureau of Valuation, or something.

The Canadian Pacific depreciates its entire group of road property as a group, and it allocates depreciation between the years on the basis of use.

THE CHAIRMAN: I am not sure of what the word "group" includes?

MR. BRAZIER: It includes all the depreciable road property, I think.

THE CHAIRMAN: The fixed property, not the moving?

MR. BRAZIER: Not equipment, but bridges, tunnels, and all that sort of thing.

THE CHAIRMAN: And station houses?

MR. BRAZIER: Station houses, sheds, and all that sort of thing.

MR. BRAZIER: Q. In getting a rate for the group, you have to measure all the component parts of that group in the terms of the unit of use that you are going to adopt?

A. That is right.

Q. So you would have to apply it to fences, as being one of the units of that group?

A. Yes.

Q. Do you think that the depreciation of fences can be related in any way to the traffic which passes over your tracks?

A. I do not have to think that way.

Q. You do not attempt to do it?

A. I do not attempt to do it. We are only thinking of a rational and systematic manner of spreading our depreciation over the years. We are not thinking of physical depreciation whatsoever.

THE CHAIRMAN: Q. Isn't that a pretty strong statement to make? You say it is a user basis?

A. No accountant, Mr. Chairman, can measure physical depreciation, and no accountant attempts to put it in his books as such. All an accountant attempts to do is to have an allocation of depreciation.

Q. And you still call it a user basis?

A. Yes. The yardstick is user.

Q. Yes.

THE CHAIRMAN: Are you finished, Mr. Brazier?

MR. BRAZIER: Yes. Thank you, Mr. Liddy.

THE CHAIRMAN: We shall adjourn now.

---At 4.55 p.m. the Commission adjourned until tomorrow, Thursday, March 2, 1950, at 10.30 o'clock a.m.

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ROYAL COMMISSION
ON
TRANSPORTATION

EVIDENCE HEARD ON

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VOLUME

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ROYAL COMMISSION ON TRANSPORTATION

OTTAWA, ONTARIO,
THURSDAY,
MARCH 2, 1950.

THE HONOURABLE W.F.A. TURGEON, K.C., LL.D. - CHAIRMAN

HAROLD ADAMS INNIS - COMMISSIONER

HENRY FORBES ANGUS - COMMISSIONER

G.R. Hunter
Secretary

P.L. Belcourt
Asst. Secretary

COUNSEL APPEARING:-

F.M. Covert, K.C. G.C. Desmarais, K.C.	)	Royal Commission on Transportation
H.E. O'Donnell, K.C. H.C. Friel, K.C.	)	Canadian National Railways
F.C.S. Evans, K.C. I.D. Sinclair	)	Canadian Pacific Railway
C.D. Shepard Wilson McLean, K.C.	)	Province of Manitoba
M.A. MacPherson	)	Province of Saskatchewan
J.J. Frawley, K.C.	)	Province of Alberta
F.D. Smith, K.C.	)	Province of Nova Scotia; Transportation Commission of the Maritime Board of Trade
J. Paul Barry	)	Province of New Brunswick
C.W. Brazier	)	Province of British Columbia

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Ottawa, Ontario
Thursday,
March 2, 1950.

MORNING SESSION

---The Commission resumed at 10.30 a.m.

MR. EVANS: Before I go on with the matter of just and reasonable rates, I want to answer a question Dr. Innis put to me yesterday at page 16764 of the Record:-

"You have not actually, or are you putting in as an Exhibit the extent to which labour is responsible for the working expenses?"

and I said on the following page that I would get that for you.

Now, I have taken the years 1940 to 1949 inclusive, and expressed the payroll as a percentage of operating expenses. You mentioned "working expenses" but working expenses include taxes and I thought perhaps operating expenses is a better basis.

In 1940, the payroll was 58.9% of operating expenses, 1941 55.35%, 1942 54.71%, 1943 51.68%, 1944 52.49%, 1945 51.76%, 1946 55.29%, 1947 54.3%, 1948 55.51%, and 1949 55.41%.

Now then, I could, if you like, give you the percentage of operating revenue if you would like that. Would you like those, sir?

COMMISSIONER INNIS: I think it would be very useful.

MR. EVANS: Then, for the same years I will just read the list, starting with 1940 and expressing the payroll in percentage of operating revenue:

43.80: 39.47: 38.85: 37.39: 41.24: 42.09: 47.83: 47.25: 50.96: and 50.89.

MR. COVERT: I was going to say if you had the dollars in both you might just give them to the reporter and they can be copied into the record at this stage.

MR. EVANS: I will be quite happy. I have not any copies.

CANADIAN PACIFIC RAILWAY COMPANY

STATEMENT SHOWING RATIO OF PAYROLL TO OPERATING REVENUES AND OPERATING EXPENSES, YEARS 1940-1949

Year	Payroll Charged Oper. Exp.	Operating Revenues	Operating Expenses
1940	$ 75,136,085	$171,535,476	$127,559,593
1941	87,818,475	222,502,518	158,655,359
1942	100,538,444	258,788,455	183,755,422
1943	111,805,234	299,023,042	216,347,579
1944	132,088,782	320,262, 132	251,646,915
1945	133,592,959	317,406,710	258,121,827
1946	140,874, 155	294,545,601	254,775,514
1947	151,790,688	321,223,099	279,520,795
1948	181,047,340	355,249,702	326,178,356
1949	184,870,924	363,252,094	333,646,392

(TABLE Cont.)

CANADIAN PACIFIC RAILWAY COMPANY

STATEMENT SHOWING RATIO OF PAYROLL TO OPERATING REVENUES AND OPERATING EXPENSES, YEARS 1940 - 1949

Year	Ratio Payroll to	
Year	Oper. Rev.	Oper. Exp.
1940	43.80	58.90
1941	39.47	55.35
1942	38.85	54.71
1943	37.39	51.68
1944	41.24	52.49
1945	42.09	51.76
1946	47.83	55.29
1947	47.25	54.30
1948	50.96	55.51
1949	50.89	55.41

Now then, I had prepared, sir, a memorandum setting out the principles which have governed the Board of Transport Commissioners at arriving at just and reasonable rates, and I apologize to my friends for putting this in at this stage, but since I have been asked for it several times, I thought your lordship would want it, and the reason I would prefer not to put in a memorandum, is that I thought some points might arise upon which you might want explanation.

Now, the first case I would like to refer to, and I won't give the citation because the reporter will have the citation, is the Granby Consolidated Mining, Smelting & Power Company Limited, decided recently to which earlier reference was made, and in that Judgment which was an interlocutory matter, the Board said as follows:

(Wardrope A.C.C. February 18, 1950.):-

> "The Board in dealing with reasonableness of rates in the many cases dealt with, has never found it possible to lay down a precise formula whereby the reasonableness of a rate could be accurately determined. In all its experience it has found, that many and varying factors enter into each case."

Now then, going to the factors that are taken into account, and the first factor that I want to mention is the ability of the traffic to bear the rate in question.

THE CHAIRMAN: You are adhering to the Board's - -

MR. EVANS: I am giving you a list of cases where the Board has taken each of these factors into account.

THE CHAIRMAN: You are going on to another case?

MR. EVANS: Yes, sir.

THE CHAIRMAN: Pardon me, when was this Granby Case?

MR. EVANS: That was decided on February 18.

THE CHAIRMAN: This year?

MR. EVANS: Yes, sir. Then, the ability of the traffic to bear a rate is a factor which the Board considers and examples of that are to be found in the case of the Montreal Board of Trade v. Canadian Freight Association and the citation of that will be in the record. ((1913) 15 C.R.C. 429). Now, that had to do with the classification of flannelette sheets. Now the classification, as your lordship knows, is the grouping of commodities in what has been called a classification, and in the grouping each commodity or group of commodities is given in a column a class to which that commodity belongs. It may be a different class for less than carload than it is for carload, but the position in the classification of each of these commodities is a matter which the Board always has to weigh and in which the sole question is reasonableness.

Now then, that case that I referred to had to do with the classification of flannelette sheets and the Board, in that Case, adopted the report of the Chief Traffic Officer and at page 432 this appears:-

> "Mr. Walsh's reference to distribution of the cost of transportation as the object of freight classification cannot be questioned; yet reductions in the ratings of articles that are able to bear the high carrying charges must necessarily tend to curtail the ability of the carrier to make rates without which the cheaper commodities cannot move at a profit".

There is the ability to bear.

Now then, a similar case was that of Horne Company v. Canadian Freight Association ((1916) 22 C.R.C. 344). That was also a classification case. The commodity was Health Salt, and the Assistant Chief Commissioner D'Arcy Scott at page 347 in the report says this:-

> "The grouping of the articles must of necessity be more or less broad... It is also elementary that in order that the cheaper goods may be carried any distance at all the Classification must be arranged according to the ability of the various articles to bear their share of the cost of transportation, so that luxuries and things that move in comparatively small quantities are rated higher than the indispensable."

Then, there was the case also of the Becker Lumber Company v. Canadian Pacific Railway et al ((1935) 43 C.R.C. 386). And that was a case in which shipments billed as fuel wood were actually used as mine props. Now, it sometimes becomes necessary to examine a commodity to see what use you make of it - -

THE CHAIRMAN: What were the articles?

MR. EVANS: These were shipments billed as fuel wood, but the shipments were actually used as mine props. They were wood, I suppose, partly logs.

THE CHAIRMAN: They were intended to be used as mine props?

MR. EVANS: They were used in fact.

THE CHAIRMAN: And that was their intention was it?

MR. EVANS: Yes, but they were billed as fuel wood apparently. Somebody apparently had decided they could get a cheaper rate by billing it as fuel wood.

Now, the Board, in that case at page 389 of the Report, which will also be in the reporter's record, said this:-

> "It has always been held, that the use of a commodity may be properly taken into consideration in determining the measure of the rate thereon." (The Board, McLean, Stoneman and Stone, at page 389).

That again is a value of service element that comes into account.

Another case, the Alberta Dairymen's Association in connection with freight rates on butter. Now, that was an application for a reduction on rates on butter on account of the drop in price of the commodity, and at page 78 (28 C.R.C. 75) this appears:-

> "The principle of charging what the traffic will bear is one of the factors which has been recognized with rate regulation. At the same time, it has not been accepted as the only factor. If a reduction in the price of a commodity is to automatically bring with it a reduction in the rate, it would logically follow that an increase in the price of a commodity would automatically carry with it an increase in the rate. This principle has not been accepted by the Board as valid. The mere ability of an article to pay, aside from the question of whether the increase in revenue to be derived from the increased rate is justifiably necessary, is not a conclusive justification for an increase in rate".

Now then, there is another factor.

The second factor is the comparison with other rates in other parts of the country, and I will not get into the question of discrimination at all. We are still on pure reasonableness. The example I first offer is Tilston v. Northern Pacific Railway and City of St. Cloud v. Northern Pacific Railway ((1899) 8 I.C.C. 346). That is rather an old case, a decision of the Interstate Commerce Commission in 1899, but it has been cited with approval by Mr. Coyne, who wrote a recent book on the railway Act and it was a Fourth Section Case, that is to say, it was a case in which the railway presumably was asking for relief under the Fourth Section of the Act, in the case of competitive rates, and your lordship will remember that one of the factors in that is to consider whether the rate to the intermediate point is in itself reasonable and that is a factor in determining whether you apply the competitive rate as a maximum at the intermediate point.

Now then, in that case Commissioner Prouty of the Interstate Commerce Commission said this:-

> "It is said that the rate from St. Cloud (St. Cloud being the intermediate point) is reasonable in and of itself. A rate can seldom be considered 'in and of itself'. It must be taken almost invariable in relation to and in connection with other rates. The freight rates of this country, both upon different commodities and between different localities are largely interdependent and it is the fact that they do not bear a proper relation to one another rather than the fact that they are absolutely either too low or two high which most often gives occasion for complaint..."

(Page16850 follows)

THE CHAIRMAN: He talks about occasion for complaint -- is that what you said?

MR EVANS: Well, he says that the reasons for complaint are usually comparisons with other rates, when you have reasonableness involved.

Then Dawson Board of Trade v. White Pass and Yukon Railway Company, (1911) 11 C.R.C. 402. This was the case I mentioned the other day. In that case Mr. Commissioner McLean said this:

"Recognizing that there are conditions peculiar to the Skagway-Whitehorse rail haul, it is at the same time of interest to make a comparison between the rates charged between Skagway and Whitehorse and the rates on the Mountain Division of the Canadian Pacific Railway in British Columbia. The class rates on this section of the Canadian Pacific are the highest in Canada outside of the Yukon."

That was before the mountain differential was removed.

"The following table gives the rates per ton for a number of commodities in both less than carlots and carlots, as well as the ton mile rates for both these classes of traffic between Skagway and Whitehorse and between Canmore, B.C., and a point 111 miles west."

Then at page 418 he says this:

"Then again, on this section, the grades are on the whole more favourable than on the White Pass and Yukon route. It may be alleged that since practically no local traffic of any consequence moves on this section of the Canadian Pacific, the class rate is simply a paper rate. This may be accepted as true, but at the same time the class rates may be taken as what the Canadian Pacific would consider to be reasonable rates if local traffic were moving over this

section. And the comparison is of some advantage in showing what is the burden of rates on the White Pass and Yukon route."

So there, in dealing with a completely removed railway, they used a level of rates in similar territory on another railway, the Canadian Pacific, just as a means of comparison.

Then there was a case of Western Ontario Municipalities v. Grand Trunk et al, (1915) 18 C.R.C. 329. That was an application for a reduction in rates on the movement of gravel. The proposed rates were sought to be justified by comparison of rates on other commodities which the railways themselves had granted, and also on the results of railway operations expressed in the per ton mile rate, as shown by governmental statistics. Sir Henry Drayton, who was then Chief Commissioner, said this:

"The Board cannot order the companies to put in an unremunerative rate, nor a rate so low as to be unfairly out of line with rates which are necessary to be maintained, in order to permit the continuance of satisfactory operation of railways, due regard being had to proper consideration of the value of the commodities shipped and the service performed."

Now we come into the third factor. This has to do with the restriction of markets. There is a case of Chouinard v. Canadian National Railways, (1937) 46 C.R.C. 218. That was an application for a reduction in rates on mill refuse, and the basis of the complaint was that the present rates amounted to 80 to 90 per cent of the value of the commodity, mill refuse. The Chief Commissioner, the Hon. Mr. Guthrie, said this, at page 219:

"On this question of the relation of the transportation cost to the value of the commodity, it may be

stated that it is not within the province of railways to dictate where manufacturing shall, or shall not, be done, or, by means of rate adjustments or otherwise, to select or control the markets where their shippers shall buy or sell. Every shipper is entitled to a reasonable rate; but, if the nature or value of a commodity offered for transportation is such as to demand an unreasonably low rate, there is no legal obligation upon the carrier to meet this demand. Mill refuse, as its name implies, is a very low-grade commodity, the transportation of which for long distances may not always be logical or practicable, and, in so far as concerns the administration of the law, the carrier has discharged its duty in this respect when it has accorded reasonable and non-discriminatory rates."

So in substance that decision merely says that, while they recognize that a low value commodity should have a lower rate, it does not lie in the Board's power to make it unreasonably low to move the traffic.

Then a case of Dominion Sugar Company v. Canadian Freight Association, (1912) 12 C.R.C. 188. The headnote contains this:

"5. Carriers are not required to adjust their rates (apart from the general question of reasonableness) in such manner as to equalize costs of manufacturing production in different sections; nor is it necessary that rates on raw material and finished products shall be so related as to tend to that result."

Then the other factor, the additional factor to which I want to draw attention, is the use of traffic statistics in testing reasonableness. An example of the use of the ton mile as a test is in the same case, Dawson

Board of Trade v. White Pass and Yukon Railway Company, (1911) 11 C.R.C. 402. There, on that subject, Mr. Commissioner McLean said, at page 416:

"While the ton mile rate is not an infallible measure of the reasonableness or otherwise of a rate, it is to be given due weight."

Then the car mile: A sample of that is Warrington et al v. Canadian Freight Association, (1919) 24 C.R.C. 155. That involved an application for reclassification of live poultry, and Mr. Commissioner Goodeve at page 158 said this:

"Dealing first with the comparison between the livestock and live poultry earnings in Official Classification territory: While it may be noted that in all cases poultry earnings per car are higher than those of livestock, I think this is justified by a consideration of the importance of the economic position of the two classes -- the very great difference in the tonnage moved, and the aggregate earnings obtained from livestock as compared with poultry."

They were trying to get the poultry rates, presumably, down to the level of the livestock rates.

Again, at page 159, Mr. Commissioner McLean said this:

"The rates as asked for on the Belleville-Toronto movement would give earnings per loaded car mile of 10.6¢; Sundridge-Toronto of 7.6¢; Brockville-Lindsay of 7.7¢; and Sarnia-Toronto of 8.2¢. These may be compared with the loaded car mile earnings for all freight for 1917 of 15.3¢. The reduction in rate, and that is in effect what is asked for, has not been justified."

They used the car mile earnings there.

Now the direction of movement: There was a case of Drummond v. Northern lberta Railways, (1946) 60 C.R.T.C.

122, a comparatively recent case. That was an application to reduce rates between sections on the line from Lac La Biche to Waterways (49 miles) to Prairie distributing scale basis the same as were applicable on other portions of the railway. Mr. Commissioner Stoneman at page 136 said this:

"Of the eight subdivisions for which tonnage originating and terminating is reported separately for the year 1945, it is evident that a balanced traffic condition exists only on the Waterways Subdivision; on the other subdivisions the outbound traffic is greatly in excess of the inbound traffic."

That shows that, although in the result they reduced the rates to the prairie level in that case, a consideration was the direction of traffic.

Then a further case of that kind is again Dawson Board of Trade v. White Pass and Yukon Railway Company, (1911) 11 C.R.C. 402, to which I have earlier referred, where Mr. Commissioner McLean at page 415 said this:

"Information for the period down to date" (information was set out from the period 1899 to the middle of 1906) "is not available to show the proportion of loaded to empty car mileage and the direction of the traffic. It does not seem necessary, however, to pursue this phase of the subject matter further, as it is a matter of common knowledge that at present the traffic is preponderatingly a one-way traffic."

Then train mile earnings were also considered. That was again the case of Drummond v. Northern Alberta Railways, (1946) 60 C.R.T.C. 122, and Mr. Commissioner Stoneman at page 137 said this:

"The first conclusion to be derived from the above table is that the 'profit' earned per train mile on the Edmonton-Waterways line for the years reported above

was greatly in excess of that obtained per train mile on the balance of the system, the net result being that the train mile earnings on the Edmonton-Waterways line contributed considerably in maintaining the system train mile net earnings level."

Now, a computation was made to show the train mile net earnings on the line in question at the present level of rates and if the Prairie scale had been in effect, and at the bottom of page 137 Commissioner Stoneman says this:

"It is noted from the above tables that the train mile net earnings on the Edmonton-Waterways line, even after the rate reduction, would still have been in excess of the net earnings on the N.A.R. in three of the six years included in the comparison, and for the year 1945, the last year for which data is available, the net earnings per train mile on this line would still be in excess of the net earnings on 'the balance of the system'.

The general conclusion to be drawn from the above comparison of net earnings per revenue train mile is that the lowering of the freight rates to the Prairie scale level would not seriously affect the net train mile earnings on the N.A.R. as a whole."

Now, from that factor we step into the characteristics of the commodity. These characteristics are the most important factor in dealing with classification, and an example of that kind of case is the Canadian National Railways v. Northern Transportation Company, (1941) 53 C.R.T.C. 148. That involved a rating on "ship partitions", and that had never been previously classified, and the analogy rule, so-called , was applied; that is to say, the ruling principle in classification cases is to find an analogy in another

commodity and to consider whether that analogy is sufficiently strong to warrant putting a commodity in the same class. Chief Commissioner Cross -- this was a 1941 decision -- at page 155 says this:

> "The rule of analogy in ordinary cases has to do with articles or things which have close counterparts in the Classification, and the application of the rule is comparatively simple. That is not so in this case, and it is very difficult to find in the Classification specific items of analogy. Under such circumstances, the rule is broad enough to involve an act of judgment enabling the prescription of a rule taking into consideration the factors such as bulk, weight, value, risk, cost of carriage, and other considerations."

Now, while dealing withthe classification cases, the Board has laid it down that it is not possible to give mathematical justice to every commodity. The classification is a result of joint conferences of shippers and railways, and by its very nature contains anomalies. A case of that kind is Planters Nut & Chocolate Company v. Canadian Freight Association, (1933) 41 C.R.C. 339. That was an application for reduced classification on salted peanuts. At page 346 the judgment says:

> "With the very limited number of classes in the Classification and the thousands of articles to be classified, the grouping of articles is more or less necessarily broad. Classification is not an exact science, nor may the ratings group a particular article by determining the yardstick, the scales and the dollar. From its very nature and use, classification cannot be so minute as to do mathematically exact justice to every variety of commerce that may move."

Another example is Muirhead Forwarding Company et

al v. Canadian Freight Association et al, (1939) 50 C.R.T.C. 402. This was a proposed classification on rubber boots and felt boots in mixed carloads. The Assistant Chief Commissioner, the present Assistant Chief Commissioner Wardrope, said at page 407:

> "The Board has, in several of its judgments, pointed out that, speaking generally, the Classification represents the work of joint committees of shippers and carriers. Having been arrived at in this manner, it follows that it contains compromises and that apparent anomalies and inconsistencies may be found."

Now, the question of onus was also raised, and this case may be of interest in that connection -- we are still dealing with reasonableness -- Board of Trade of Moose Jaw et al v. Canadian Freight Association, (1928) 34 C.R.C. 362. The Assistant Chief Commissioner, Mr. McLean, near the bottom of page 370, says this:

> "A toll established in the first instance by a carrier of its own volition and having remained some time in force is, presumptively, reasonable; and the onus is on the carrier to show, with reasonable conclusiveness, that changed conditions or increased costs of prices justify an increase."

And I think it could be said it follows that if it is presumptively reasonable for the carrier, it is also presumptively reasonable for the shipper, and if the shipper is attacking a rate which has been in effect the onus would then be on him. If the railway wants to change the rate upward, then the onus is on the railway. I think it is important to bear that distinction in mind. The onus in matters of reasonableness is not the same as it is in matters of discrimination.

Under section 319 of the Railway Act -- I might put this is the context, just to point up the distinction in the case of reasonableness and in the case of discrimina-- tion so far as the question of onus is concerned. The section reads:

"319. Whenever it is shown that any railway company charges one person, company, or class of persons, or the persons in any district, lower tolls for the same or similar goods, or lower tolls for the same or similar services, than it charges to other persons, companies, or classes of persons, or to the persons in another district, or makes any difference in treatment in respect of such companies or persons, the burden of proving that such lower toll or difference in treatment does not amount to an undue preference or an unjust discrimination, shall lie on the company."

So you could have this kind of situation: First you show a difference in tolls. Now, the onus would then be on the railway to show that that did not amount to unjust discrimination. Now, supposing that the finding were that it did not; if anyone then wants to attack the reasonableness of the rate, having filed a discrimination count, the onus is on him who attacks it; if it is a complaint by a shipper the onus is on him if the rate has been in effect for some time; and, similarly, if the railway wants to change it and it has been in effect for some time, the onus is on it. I think perhaps that would clear up that point of onus.

Now one other case -- it is one to which I have already referred, but it is on the same point of onus: Dominion Sugar Company v. Canadian Freight Association, (1912) 12 C.R.C. 188. Headnote 4 in that case reads this

way:

"4. Where special circumstances have operated for a time, e.g., effective water competition, to induce a carrier to give a lower rate, the burden of proving unreasonableness is not necessarily upon the carrier when the rate is subsequently increased."

Now, that is a distinction to be made in the case of competitive rates. In other words, if the rate has been competitive and the railway wants to change it, then of course the rule of onus does not apply, because one does not presume that a competitive rate is the reasonably high level for a rate to be, because that involves competition, so that that distinction can be borne in mind.

I have said all I have to say on the subject.

THE CHAIRMAN: Thank you, Mr. Evans. Do we go on now with Mr. Liddy's examination? Mr. Shepard, have you something to say?

MR SHEPARD: I am going on with Mr. Liddy in a moment, sir.

MR SINCLAIR: There was a question yesterday, my lord, concerning reduction in passenger train service. The question arose at page 16807 of the transcript, volume 86. I have made enquiries, and I find that, while there is no statutory requirement or any order of the Board requiring a railway to secure an order for reduction of passenger train service, the practice is that where passenger train service on a given portion of the line of railway is to be abandoned completely, they always get an order of the Board.

(Page 16862 follows)

If passenger train service is merely to be reduced from the .service already in existence all that is required is that notices should be published in the stations and other places in accordance with circular 139 of the Board of Transport Commissioners. Always, of course, any reduction is open to complaint and section 312 of the Railway Act requires that adequate service must be rendered by the railways and if a complaint is made on a reduction of passenger train service the matter is gone into by the Board.

THE CHAIRMAN: Must these notices be published a given time before the cessation of the service?

MR. SINCLAIR: Yes, the regulations and where it is to be publi .hed and the time and all that are set out in that circular of the Board.

S. J. W. LIDDY, Recalled

CROSS-EXAMINATION BY MR. SHEPARD(Cont'd):

MR. SHEPARD: Mr Chairman, the Commission will rrmember that/when I was asking certain questions of Mr Crump he indicated that he would prefer to have some of them answered by Mr Liddy I propose first, therefore to ask Mr. Liddy to turn to page 5 of part one of the C P.R Submission.

THE CHAIRMAN: What page?

MR. SHEPARD: Page 5 of Part I, sir.

Q. Paragraph 20, Mr. Liddy, is the top paragraph on that page, and it is one that I did discuss to quite a considerable extent with Mr. Crump, but there were two or three questions that I wanted to ask with reference to the last sentence which reads:

" The increase in efficiency has been possible because heavy capital expenditures have been made

[illegible]

[illegible]

[illegible]

[illegible] Mr [illegible]

by the company."

The first question I wanted to ask you, Mr. Liddy, was whether you could tell us if the capital expenditures per ton mile have increased between 1885 and 1948?

A. You mean, Mr. Shepard, is the value of our property to-day in relationship to the traffic moving in ton miles greater or less than what it was in 1885?

Q. Yes?

A. I think our digest of development ought to indicate that, Mr. Shepard.

Q. Can you give me the chapter and verse as to where I would find that? That is page 27 of the Appendix to Part I?

A. Yes, Mr. Shepard. In 1885 the net railway property investment account was $160 million.

THE CHAIRMAN: Q. Pardon me, what column?

A. That is the second column, sir.

Q. Net railway property investment?

A. $160 million for the year 1885, and the revenue freight ton miles for that year were 406 million, and in 1948 the corresponding figures are for net railway property investment $1,031,000,000, and the revenue freight ton miles 25,000,000,000.

MR. EVANS: Q. Then you divide one into the other?

A. Yes. Have you done that, Mr. Shepard?

MR. SHEPARD: Q. No, I have not.

A. Do you want me to do that here?

Q. No, I do not want you to make the calculation, but just from looking at it, and I am not too good at arithmetic, it appears that the ratio is about the same as it was then. If you divide one into the other in 1885 and repeat the process in 1948 --

THE CHAIRMAN: You say the ratio is about the same?

MR. SHEPARD: It would appear to be about the same. I have not made the calculation.

MR. EVANS: There is one rule of thumb there. The capital has gone up in the relationship of 160 to 1,031 which looks to be about eight times, and the ton miles have gone up about 60 times.

MR. SHEPARD: Yes, that is quite right, but comparing the two columns, net railway property investment and revenue freight ton miles in the two years, would you agree, Mr. Liddy, that the ratio appears to be about the same?

THE WITNESS: Yes, I think it is approximately the same, Mr. Shepard.

MR. SHEPARD: Q. Then, can you tell me whether there have been any heavy capital expenditures since 1930 by the C.P.R.?

A. It appears from this exhibit that the increase in capital expenditures has been offset by the increase in the depreciation reserves which, of course, have been growing.

Q. But as far as actual capital outlay is concerned since 1930?

A. Yes, we spent quite a lot of money.

Q. Have there been any particular investments or expenditures that you would classify in your own thinking as heavy expenditures?

A. Yes.

Q. Can you perhaps give us some illustrations of those?

A. Well, may I just speak generally?

Q. Yes, surely.

A. Take our locomotives, for example. They are quite a heavy expenditure. To-day we are paying for new locomotives anywhere from $150,000 to $250,000, and these new locomotives are replacing older power costing $20,000 --

THE CHAIRMAN: Q. What is that?

A. These new locomotives are replacing older power costing from $20,000 to $30,000. It is true that the new locomotives to-day probably are double the capacity, but they are not five times the capacity. We have also made capital expenditures in heavier rail in order that we may use heavier power. We have also improved many of our facilities, our yards, our roundhouses, our turntables, in fact all our appurtenances that enable the railway to take advantage of the efficiency that can be obtained by hauling a longer train and using just one train crew, and so forth.

MR. SHEPARD: Q. I suppose you would agree with me though, Mr. Liddy, that the bulk of your capital expenditures as a railway company were made before 1930? I think that is probably pretty obvious from the figures?

A. Oh, yes, the Canadian Pacific Railway system in 1930 consisted of 15,000 miles, and it has only grown 2,000 miles since then.

Q. Yes, that is right. Then would you care to express any opinion as to whether you think the capital cost per ton mile in the future will be higher than it has been in the past?

A. My opinion would be it will rise substantially.

Q. It will rise substantially?

A. Because our present capital investment represents prices on the average of 35 years ago or 40 years ago, whatever the life of these assets may be, and as those assets wear out and are replaced by new assets the new

cost at higher prices will come into effect.

Q. Well, a part of the increase of course would be accounted for by the proposed $400 million program?

A. Part of the increased price?

Q. No, part of the increase in your capital investment?

A. Oh, that is a part of the program.

Q. It is true what you are purchasing there is at higher prices than you would have paid if you had made the purchases before the war. You are actually intending to increase your plant capacity by this improvement program?

A. Well, as an accountant I am not very familiar with that program.

Q. I am not going into the details of that with you.

A. But there has been a steady growth, small it is true, in our traffic volume over the years, and I think Canada still has a future, and that the traffic of this country will grow, and that we must expand our railway facilities to meet that traffic growth.

Q. And I presume you share the view of other C.P.R. officials --

THE CHAIRMAN: Pardon me a moment. Is there justification for using the word "program", Mr. Evans?

MR. EVANS: We refer in our brief, as you will recall, to a capital program over the next five years of $400 million, and savings from that were to be given by Mr. Newman who will be in the witness stand in due course.

THE CHAIRMAN: Yes, I remember the origin of that statement, but it can be called a "program" from now on?

MR. EVANS: Yes, it is a program.

THE CHAIRMAN: You refer to it in your brief?

MR. EVANS: Yes.

THE CHAIRMAN: Do you remember about where in your brief -- oh well, you can give it to me later.

MR. EVANS: It is right near the beginning. It commences about page 8 of Part I and runs on to page 15.

MR. SHEPARD: Q. I think, Mr. Liddy, I was just asking you this question, that I presume you share the view expressed by other C.P R. officials that there will continue to be an increase in traffic volume?

A. That is my view, but you are taking me out of my accounting field, and I do not like to get outside my books.

Q. Well, I will see if I can get you back in them. Before I go on, Mr. Evans has handed me a computation that one of his experts has made. The net railway property investment per ton mile -- that is along the line I was discussing with Mr. Liddy with reference to the two columns on page 27 of Part I of the Appendix -- in 1885 was $395 per thousand --

THE CHAIRMAN: How much?

MR. SHEPARD: $395 per thousand, and in 1948 $40 per thousand. I am not too sure about this. Perhaps Mr. Evans can explain it. That is per thousand gross ton miles.

THE CHAIRMAN: The first figure is what?

MR. SHEPARD: $395.

MR. EVANS: Revenue ton miles; you are using page 27 of the Appendix. You have those two columns and all we did was to calculate the relationship which you asked Mr. Liddy about, and which he had not previously calculated. We used 1885 and 1948 and got that relationship.

MR. SHEPARD: Then the net railway property investment per revenue ton mile in 1885 was $395 per

thousand revenue ton miles, and in 1948 was $40 per thousand revenue ton miles.

Q. Then, Mr. Liddy, on page 15 of Part I of your submission, paragraph 22 of the outline submission deals with the question of the ratio of net to gross earnings, and this is one of the subjects that Mr. Crump said he would prefer that I discuss with you. I suppose you would agree that as the revenue increases through increased volume of traffic that you would expect the ratio of net to gross to diminish?

A. If other factors remain constant and we had not reached or nearly reached our absolute capacity.

Q. Then your answer would be yes?

A. Correct.

Q. Paragraph 23 which is very short reads:

> "If Canadian Pacific is to continue to give low cost efficient transportation, a reasonable ratio between net and gross earnings must be provided."

Would you care to express an opinion as to what would be a reasonable ratio?

A. One cannot be too dogmatic about a reasonable ratio, but I would like to refer the Commission to Exhibit 190 which appears at page 27 of the appendix, and particularly to column 9 --

THE CHAIRMAN: Column 10 -- are you including the date column?

THE WITNESS: 10 including the date column.

THE CHAIRMAN: What is the heading?

THE WITNESS: The heading reads "Ratio net to gross earnings", and while the paragraph that you have just read to me, Mr. Shepard -- no, that paragraph also speaks of the relationship of net to gross.

MR. SHEPARD: Q. Yes.

A. It is the same factor as covered in this column 9, ratio net to gross. It will be observed that for more than one-half of the company's history the ratio of net to gross exceeded 30 per cent. Then we get down to the period 1918, 1919, 1920, when the post-war prices of materials and labour increased.

(Page 16870 follows)

Q. And competition increased too?

A. And the Canadian National began to be a strong competitor of the Canadian Pacific.

Q. And other forms of transportation?

A. Other forms, and the ratio then declined drastically and it is only with the growth of the country, the growth of its industrial activity, that we are now or should now be coming back to what I consider to be a reasonable ratio which is somewhat about 30%. I would refer you, Mr. Shepard, to the Judgments of the Board of Transport Commissioners wherein they found that the Canadian Pacific were entitled or should have net earnings of the order of $50 million - $49 million in one Judgment, $54 million in another judgment.

Now, if you calculate that ratio, you will find that it works out to over 30%, about 31 to 32 or 33% and with my historical knowledge of the Canadian Pacific and its needs, it is my view that a reasonable operating ratio or rather a reasonable ratio of net to gross earnings should, at the present time, be slightly in excess of 30%.

Q. Now, are you referring to the recent rate cases when you refer to the $50 million and the $54 million?

A. That is right.

Q. And you say, that the ratio of net to gross earnings resulting from a net earning of $50 million to $54 million to day's volume of traffic would be about 32%?

A. Well, not quite on today's volume.

Q. But I took it from what you said, that you were content that a $50 million to $54 million net earning be allowed. If you applied that to your gross earnings

of 1948, which, it runs in my mind, were around $355 million (I am not sure of that because I am speaking from memory).

A. That is about right for 1947.

Q. Well, what kind of a ratio would that work out to? Itwould not be 32%?

A. That is about 27.7% operating revenue, but that is a very high traffic volume at the present time.

Q. But you expect it to be higher?

A. Not just immediately. Take our operating results for January. I think they show a decline of something like 15%. I think we are in a very high traffic volume period just at the present time.

Q. Well, assuming today's traffic volume, Mr. Liddy, would you care to name a figure as, in your opinion, a reasonable ratio? That is what you have referred to in Paragraph 23 on page 15, and that is really what I was interested in discussing with you.

A. Well, that depends on the period you are in.

Q. I am assuming today's present traffic volume and today's conditions?

A. I think the minimum ratio would be what the Board found.

Q. Whatever that may work out to?

A. Personally I do not think it was enough, but I would take that as a floor.

COMMISSIONER INNIS: How does this compare with Class I American Railroads?

A. They have a better operating ratio than we have, sir.

Q. Has there been the same general trend of decline?

A. Yes, they have declined somewhat, but they got

their freight increases more frequently and quicker than we did. I have a figure here for the year 1948 which shows that United States Class I Railways earned a 4.24% rate of return on their investment which compares with our 1.80%.

Q. You have not a figure on the ratio?

A. No, I have not the ratio.

COMMISSIONER ANGUS: This matter of ratio, if the labour costs of the railways rose sharply, as they have done, would you expect your ratio of net to gross to remain constant, I mean expect to be kept constant? Would your net return increase because your labour costs increased?

A. Well, perhaps not immediately, Dr. Angus, but I would think over a period of years it should increase because labour costs are merely a reflection of the price levels and your property investment will go up with price levels, your need for capital expenditures - -

Q. I was wondering whether you were really thinking in terms, if I can put it rather crudely, of cost plus percentage or cost plus fee?

A. I think, looking back over the history of railways over many years, that it is the ratio that finally wins out - not dollars. Dollars are fluctuating things; a dollar is worth so much today and worth half as much as fifty years ago. I think the ratio is the firmest basis we have of measuring what is a reasonable return, - one of the yardsticks anyway of measuring what is a reasonable return.

Q. But a lot of your costs are in dollars, these fixed charges and so on that do not change with the

vintaging of the dollar?

A. That is true, Dr. Angus, but financial obligations have a habit of maturing and being replaced, and people expect dividends that will do some purchasing for them.

Q. Can perpetual 4% consolidated debenture stock change?

A. No, we have a very good security in that consolidated debenture stock. That is one of the exceptions, Dr. Angus.

MR. EVANS: It does not always sell at par.

MR. SHEPARD: Then, Mr. Liddy, would you turn to page 16, the top paragraph there, paragraph 25:-

"25. Canadian Pacific submits basic economics supports the proposition that the cost of rail transportation, including the wages of capital as well as labour, should be borne by the traffic which moves over the railway."

Now, I think perhaps as a starting point, that I would agree with that statement, underlining the word "should". In other words, it is theoretically correct that the cost of railway transportation, including the wages of capital as well as labour, should be borne by the traffic which moves over the railway, but then I wanted to discuss with you what might transpire if things worked out that they could not be borne according to these basic economics that are expressed in the paragraph?

A. You mean, we would go into a bankruptcy or something?

Q. Well, I might get to that in a minute, but I wanted you to envisage with me, the possibility that railways might lose traffic, as they have in the past, to competitors

and that you would not be able to decrease your costs sufficiently to hold your present net operating position. Would you agree that that is a possibility?

A. Well, I am getting outside my book again, Mr. Shepard. It is really an economic question, but personally I am a firm believer that a steel wheel on a steel rail will provide low cost transportation for many years to come - a steel wheel on a steel rail.

Q. Well, I am inclined to agree with that statement, Mr. Liddy, but I just wanted you, if you could, to come along with me and assume that competition from any source you might care to think of might have the effect of reducing the railway gross earnings and that you would, because of increasing costs of material and labour, be unable to reduce your operating expenses sufficiently to hold your present net operating position. Now, if that should transpire, have you any suggestions as to what might be done about it?

A. That is out of my field really, Mr. Shepard.

Q. That is fine; I don't want to pursue the matter then.

MR. EVANS: Before you go ahead, Dr. Innis asked about the ratio for United States Railways, and I find that it is in page 13 of our Appendix, the same ratio of net railway operating income to operating revenue for a period from 1888 to 1948.

COMMISSIONER INNIS: This one lumps them altogether?

MR. EVANS: Yes.

COMMISSIONER INNIS: There has been a very perceptible trend downwards?

MR. EVANS: Oh, yes, they had a period during

[illegible] old, come [illegible]

[illegible]

[illegible] but I must [illegible], for some [illegible]

[illegible]

[illegible] would [illegible]

[illegible]

[illegible]

which a great many of the very big systems were in bankruptcy in the 30's.

MR. SHEPARD: Now, Mr. Liddy, going back to page 16 again, I have just one or two more questions I should like to discuss with you. Mr. Brazier was asking some questions yesterday about passenger traffic, and whether it was making or losing money. I just wanted to get your opinion, again based on that assumption which I do not want to become involved in a discussion with you about, and that is this, that if the passenger traffic is in fact losing money, and it can be proved to your satisfaction and my satisfaction, do you consider it is fair that those losses should be borne by other freight payers or by the freight payers?

A. If you want transportation, some person has got to pay for it.

Q. I am just asking you about the fairness of that?

A. Well, I think that would be fair. If I want something, if I want transportation, which is shipping my goods and taking care of my travelling needs, then I think it is only fair that I pay for it.

THE CHAIRMAN: I do not think the question has been put, what about passengers paying a more equitable share?

MR. SHEPARD: Well, I have assumed, sir, that it is impossible to raise the passenger fares because of competition.

MR. SINCLAIR: The evidence, my lord, from the traffic officers of the Canadian Pacific was that the passenger fares cannot bear anymore increases because they would get into a position of financial returns. The level

has reached the maximum that can be applied to the demand.

MR. FRAWLEY: I think it is only fair to say, that if that statement was made by Mr. Warren, the Chief Passenger Traffic Officer of the Canadian Pacific - he did say what my friend Mr. Sinclair said - but after that they took a 15% increase just about a year ago, and seemed to take that in their stride.

MR. O'DONNELL: It would be fair, also, to say that that was merely the tax that had previously prevailed, the Dominion Government Tax and it waived that and allowed the railways to take it but the level of the passenger fares did not increase at that point.

MR. FRAWLEY: Simple expedient.

MR. O'DONNELL: Well, there were more taxes to be raised.

THE CHAIRMAN: Am I right in this, that the railways appear to have taken the attitude that they cannot call upon passenger traffic to increase their revenue?

MR. SHEPARD: That is true, sir.

THE CHAIRMAN: I should not ask Mr. Liddy that, but that appears to me from what you say, Mr. Sinclair?

MR. SINCLAIR: That, sir, is the view of the traffic officers of the Company.

COMMISSIONER ANGUS: Does that mean that the passengers have to be condemned to move by bus or else subsidize by somebody ?

MR. SINCLAIR: I think the view of the railways in that regard, Dr. Angus, might be, that the bus fares are depressed below where they should be because they are not paying all the factors that should come into their cost picture, so that actually they are being subsidized

by the people generally.

COMMISSIONER ANGUS: Subsidized by what?

MR. SINCLAIR: By not having to bear the full cost of the maintenance and construction of highways.

COMMISSIONER ANGUS: They dispute that, don't they?

MR. SHEPARD: Very much so.

COMMISSIONER ANGUS: Then assuming that that is true, if that situation exists the railways would be conceivably in this position, that they might effect economies by cutting down services if the passengers cannot be condemned to move by bus or not moved at all, and that the alternative to that seems to be subsidizing the movement of passengers either from freight rates or some other source?

MR. SINCLAIR: Of course, this is all on the assumption put by Mr. Shepard, and that is, that the passenger rates were a loss-rate, and the evidence, I think, of Mr. Walker and Mr. Liddy, was that they were paying their out-of-pockets costs and were contributing something to the overhead expenses, and so, therefore - -

THE CHAIRMAN: Have we had evidence to that effect?

MR. SINCLAIR: Mr. Walker said that that was his view. He said there were different views and that was his, and, I think, that Mr. Liddy said that he felt that it contributed something more than their out-of-pocket costs.

MR. SHEPARD: My recollection, sir, of Mr. Walker's evidence was, that he indicated that he could not tell; there were too many arbitraries involved.

THE CHAIRMAN: Does Mr. Sinclair's present

statement agree with this Exhibit which has been filed?

MR. SINCLAIR: I think so, my lord. I think Mr. Liddy explained that.

MR. EVANS: He said yesterday in examination-in-chief, that the out-of-pocket costs would lie somewhere between the figure of directly allocable expenses and the total figure, and he thought they would lie nearer to the directly allocable expenses than the total figure, and, as I recall the Exhibit, the directly allocable expenses were $39 million, and the revenue in the same Exhibit was $62 million. I do not think anybody said exactly where they lie, but there is that amount of evidence.

THE CHAIRMAN: But then, of course, you just give on the one hand the identifiable costs?

MR. EVANS: Yes.

THE CHAIRMAN: And you do not mention the apportioned costs?

MR. EVANS: Well, it is between. You see, on Exhibit 180, the expenses solely related to passenger traffic are shown for the year 1948 as $39 million odd, and the apportionments are $52 million odd. Now, some part of those that are apportioned are out-of-pocket according to Mr. Liddy. His view, as he expressed it in chief, was, that the true figure of out-of-pocket costs would lie nearer the $39 million than it would to the 91 million in the Exhibit.

COMMISSIONER ANGUS: But was not the evidence also that the passenger traffic was much more remunerative on main lines than on branch lines?

MR. EVANS: There may have been some evidence of that kind.

MR. COVERT: Mr. Chairman, I thought it might be a good time to bring this point up because it has been

confusing me a little. As I understand it, if the $52 million which has been apportioned happens to be the right figure, that would mean, I take it, that $91 million should be attributed to passenger services. Is that correct?

MR. EVANS: If it is the right figure for the true cost, yes, but I think I ought to qualify that, Mr. Covert, because I do not want there to be any confusion. The $91 million represents the total apportioned costs as near as a statistical cost accounting office can verify. It does not mean you can save that $91 million by stopping passenger traffic.

THE CHAIRMAN: Pardon me, Mr. Covert. I notice you use the phrase there "out-of-pocket costs"?

MR. EVANS: Yes.

THE CHAIRMAN: Now, in what sense do you use that this time? You see, we were told before there in one of your paragraphs that "out-of-pocket costs" in that connection meant the additional costs?

MR. EVANS: We use that term "out-of-pocket" as meaning incremental or additional costs, but there is a difference, as perhaps your lordship will remember was pointed out in my cross examination of Mr. Brown. The Interstate Commerce Commission tends to get the two confused. They are not exactly the same, but we have used that in the sense of incremental costs. Sometimes incremental costs - -

THE CHAIRMAN: You are saying "implemental"?

MR. EVANS: No, incremental, the increment of cost. The increment of cost for a given amount of traffic is lower than the average variable or out-of-pocket cost.

When the amount of variable costs is on a downward trend, the marginal or incremental costs tend to be lower than the average variable costs, and when they are on an upward trend the reverse is true, but it is a distinction perhaps that is too fine to make in figures.

THE CHAIRMAN: You cannot find different formulae for expressing the idea, because sometimes you use out-of-pocket costs apparently in a different sense than what you are using it now?

MR. EVANS: Well, I was giving you what is the true scientific definition.

THE CHAIRMAN: I am not quite sure that I assimilated the explanation.

MR. EVANS: May I put it this way? If you were to find in a given situation, that the average variable costs were at a certain level, that is to say, the costs which vary with traffic represented so much percent of the total costs, now, if you find the trend of that variability upwards getting nearer to 100%, then you would find that for each additional traffic added the marginal or incremental costs would tend to be higher than the average variable costs. You see, if you are only increasing an average it is going upward, and you have got a real inertia in the average, if I make that clear, and you will find your marginal costs for a given increment of traffic higher than the average and similarly if your trend is downwards, you will find your incremental costs slightly lower than the average. I think Dr. Angus is following it. I am so abstruse on it.

THE CHAIRMAN: You are not abstruse at all.

MR. COVERT: Mr. Chairman, the point I wanted to bring out on that was this, because I have been confused on it right along, and that is they say that the actual expenses solely related to passenger are $39 million odd, and then they apportion statistically $52 million odd, making a total of $91 million. Now, Mr. Liddy said, that in his opinion, the actual out-of-pockets costs were somewhere nearer the $39 million than they were the $91 million. Now, my point would be, that if you take half of the $52 million or slightly less than half and add it to the $39 million, you would get approximately $64 million. Now, that would be closer to the $39 million than it would be to the $91 million, but there would still be not enough remuneration. I wanted to know if I could, what does it mean by "closer to the $39 million" because, as I say, $64 million would still be closer to $39 million than it would to the $91 million?

THE CHAIRMAN: Then, is the general position of the Canadian Pacific this, that passenger service is now paying the out-of-pocket costs and in addition contributing something to the general revenue?

MR. EVANS: I do not think we can take that position flatly, because we frankly do not know, but there may be losses in some years - -

THE CHAIRMAN: I thought you said Mr. Walker said that?

MR. EVANS: He said merely that his view was, that it was paying out-of-pocket costs. I don't think anybody has made a study.

THE CHAIRMAN: It is your views that I want. I want to know the position. Of course, we all know that

you don't know.

THE WITNESS: Well, what I meant, Mr. Covert, in saying it was my view that the out-of-pocket costs were closer to $39 million than what they were to $91 million was, that the out-of-pocket costs, including the $39 million, that is - - I would like to make a fresh start. Let us assume, for example, that the out-of-pocket costs involved in the $52 million is $20 million.

THE CHAIRMAN: Involved in the what?

A. $52 million.

Q. Is how much?

A. Is, say, $20 million. This $20 million added to the $39 million gives you a figure that would permit some margin of revenue over out-of-pocket costs.

Q. What kind of costs are not out-of-pocket?

A. Well, take my salary, Mr. Chairman.

MR. FRAWLEY: With the income tax on it?

THE CHAIRMAN: I don't know how literally you want me to take it.

THE WITNESS: If you can find my salary, my salary would probably go on whether or not we had any passenger business or not.

THE CHAIRMAN: Then, in respect to passenger business, it is not an out-of-pocket cost?

A. That is right.

Q. And then you get thrown back onto this apportionment, don't you? It is part of the $91 million?

A. Yes, my salary is pro rata.

Q. Then, we drop back to the definition. I can't put my finger on the page, but the other day you said the out-of-pocket cost is the additional cost. It struck

me as a curious definition, but there it is, and the out-of-pocket cost, that is to say, the additional cost of providing a certain service. It seems to me a strange definition, but there it is. Do you remember it, Mr. Evans?

MR. EVANS: Yes, we quite clearly used the definition of out-of-pocket costs as being synonomous - -

THE CHAIRMAN: Can you refer me to the page of your Brief where you use it in that sense? I have it, Mr. Evans. For instance, at the top of page 70 and the beginning of page 71, you say:-

> "There is an assumption that competitive rates in Eastern Canada and particularly in the provinces of Ontario and Quebec are unreasonably low and in some cases at least do not pay their out-of-pocket costs".

Now, that is one thing.

MR. EVANS: Yes, sir.

THE CHAIRMAN: At the head of page 62, you say:-

> "Under the value of service, consideration must be given to the compensatory nature of the rates. A rate is compensatory if it returns something more than the out-of-pocket costs which are the additional costs incurred by the railway in handling any particular traffic?"

MR. EVANS: Yes.

THE CHAIRMAN: Now, supposing the particular traffic/here is passenger, would this not still have the same meaning?

MR. EVANS: Yes, but in other words, you would have it in reverse. If you took off the passenger traffic,

how much would you save, or if you put on the passenger traffic, how much would you add?

THE CHAIRMAN: What you save by eliminating certain services is out-of-pocket costs?

MR. EVANS: Yes, or if you add traffic, what you would add to the cost and what you eliminate if you take the traffic off . That is strictly speaking out-of-pocket, but the confusion comes (it did in my thinking) when we were talking about average variable costs, and there is a distinction between average variable costs, that is averages that vary with traffic and the incremental costs, or as we call it, out-of-pocket costs.

THE CHAIRMAN: Well, we will think that over.

...RECESS

(Page 16883 follows)

---Upon resuming:

COMMISSIONER INNIS: Q. It seems to me, Mr. Liddy, that yesterday you went much further than you are inclined to go now, when you said that a dollar earned on passenger traffic was a dollar added to net earnings; was that a misunderstanding?

A. If we can pick up an extra dollar, I think you will find that drops right into net earnings.

THE CHAIRMAN: Q. Why do you call it an extra dollar?

A. An increment, sir. I am only pointing out that there may be an impression that passenger business is not important.

Q. Is what?

A. Is not important, and that we should let it slide. I merely want to point out that from a practical standpoint, if you can pick up a hundred dollars of an extra fare of a passenger going from Montreal to Vancouver, go after it and get it; it is a hundred dollars, and your cost of carrying that passenger is practically nil.

Q. But you have provided the facilities for carrying him?

A. Sure we have; we have those facilities, and we have got to provide that service.

COMMISSIONER INNIS: Q. That would only apply at the upper levels; if you push that to its absurd conclusion it would mean that the whole passenger business was greater, and you could charge all your costs---

A. No, I am assuming under my example, Dr. Innis, that we have a train going to Vancouver and we have a seat and we have a car, and if we can pick up another passenger we are going to go right after that passenger.

Q. Oh, yes, I understand that.

A. And if we lose him we are out a hundred dollars.

Q. I was just wondering how far you wanted to push that?

A. I do not want to push it to the absurdity.

MR SHEPARD: Q. Then, Mr. Liddy, going back to page 16 of Part I again, paragraph 25, dealing with the wages of capital, I just had one or two further questions on that. First of all, it is a matter of historic fact, I think, that the C.P.R. did obtain land grants, grants in aid of construction, donated road and cash subsidies in their early history?

A. That is right.

Q. And in that respect the C.P.R. is perhaps different from an ordinary corporation which obtains its original capital from the sale of securities -- I do not want you to commit yourself to anything, but at least to that extent, other corporations are not in the same position?

A. Well, that is a long subject, Mr. Shepard. You ask me if we are in any different position than an ordinary corporation. An ordinary corporation, it is true, probably did not have the benefit of those grants.

Q. Well, that is as far as I wanted to go into the subject.

A. But may I point out that an ordinary corporation would not have done what the C.P.R. did. They would not have built a railway across Canada when there were only a few hundred settlers west of the Great Lakes. Now, an ordinary corporation when it wants to set up business makes a decision that there is money in that business and goes after it, so that, while your question may appear simple on the surface, I just cannot quite say ---

Q. Yes or No?

A. ---Yes or no to that question. They are not

similar.

Q. Then the last question that I wanted to ask you is -- and I have now led up to it -- do you consider that the traffic moving over the railway today should pay the wages of that portion of your capital which was not provided by the owners of the railway?

A. Now, could you make that a little plainer for me?

Q. Well, perhaps I could re-phrase it this way: Do you consider that wages of capital, to start with, I presume, are a return on capital? That is the meaning of that phrase?

A. I would think -- I did not write this section, it is not my section, but---

COMMISSIONER INNIS: How do you distinguish that from interest, Mr. Shepard?

MR SHEPARD: Well, I would like someone else to answer that question, sir.

MR EVANS: Would you like me to answer it?

MR SHEPARD: I would be delighted.

MR EVANS: I do not think it is really distinguishable. Take the simple case of a taxi driver, whose father gives him ten taxis. Is it to be argued that he is not to be allowed a return on that investment of those ten taxis because his father gave it to him? To me it is as simple as that.

COMMISSIONER INNIS: Why not call it interest?

MR EVANS: Well, it may be interest if he owes interest, but it is not interest; it is a return to him if he has put up the money or if his is the equity.

COMMISSIONER INNIS: It seems to me there is a tendency to raise the term interest to the same level as wages.

MR EVANS: Well, wages in the sense of a return

to him who provides the capital. The taxi driver who has got the ten taxis given to him is providing the capital.

COMMISSIONER INNIS: Then you would have the capitalist trying to pretend that he is a labourer.

MR EVANS: Well, perhaps there are distinctions, but in effect you cannot hire capital unless you pay a wage for it. It takes the form of a wage on borrowed money or a return on equity money which is not borrowed and not repayable.

COMMISSIONER INNIS: Yes. It is merely quibbling over phrases.

MR SHEPARD: Q. Mr. Liddy, my question then is, assuming that wages of capital might be considered to be either interest or a return on investment, do you consider that capital that you have not hired yourself, to use Mr. Evans' phrase -- in other words, it has been handed to you -- should be entitled to earn a return out of the freight dollar?

A. Capital handed to the Canadian Pacific?

Q. Yes; and by that I am referring now to land grants, grants in aid of construction, donated road and cash subsidies.

A. Oh, I don't understand this business of "handed to" at all. Do you mean put on a platter?

Q. Well, I had not a platter in mind, but -- you agreed with me a moment ago, I think, Mr. Liddy, that those were assets that the C.P.R. acquired without paying for them?

A. Oh, I beg your pardon, I never said anything like that.

Q. Well, perhaps you could tell me what you did say?

A. Not since I was a little fellow, at all. May I refer you to Mr. Walker's statement?

MR FRAWLEY: Q. The one that has been printed and circulated?

A. Well, he gave evidence here; it is in the case. I won't read it all, because the Commission are quite familiar with it.

THE CHAIRMAN: I am not so sure.

THE WITNESS: I quote: " . . . and further declares that when the contract for its construction is performed the Canadian Pacific Railway shall become and be thereafter the absolute property of the Company."

MR SHEPARD: Q. Oh, yes, there is no question about that.

A. And it was under contract for terms which we fulfilled and which we worked for and sweated for, and to say it was handed to us -- I just don't understand that language at all.

Q. Well, that is fine; I wanted to get your thinking straight on that.

THE CHAIRMAN: Q. Apparently Mr. Walker takes this position, that once the railway was built, all the prior conditions of its building might just as well be forgotten -- I am not criticizing that; I just want to get at his attitude -- that from then on the railway as built has become the property of the company, probably in the same way as Mr. Evans exemplified a while ago, by somebody whose father gives him a number of taxis and says, "Go on and operate them," or who inherits, as he might do, a number of taxis and starts to operate them. From the time that this declaration became effective the company then should simply be considered as a carrier with certain services to offer and expecting remuneration reasonable having regard to the service provided, without raising any question about how it obtained its property. Is that it?

A. Well, that is our position, but those are not the reasons, sir.

THE [illegible]: [illegible] ... the [illegible]

[illegible] to [illegible]

[illegible] will become [illegible]

[illegible] property of the [illegible]

[illegible]

And it is [illegible] order contract for [illegible] worked for [illegible] I [illegible]

[illegible], that is fine: I [illegible] your [illegible] it.

THE [illegible] (gently) [illegible] was built. [illegible]

[illegible]

THE CHAIRMAN: Mr. Evans, is that it?

MR EVANS: Well, I would think so, but I would go a little further; I would say that we gave very substantial considerations for these properties.

THE CHAIRMAN: Yes, but, you see, all that is merged, it appears to me, on both sides. You gave and you received, and at a certain time then that came to an end. Here was a railway; now it is yours. Then from now on you offer your services to the public for valuable consideration.

MR EVANS: Yes, sir.

THE CHAIRMAN: At reasonable rates.

MR EVANS: Yes, sir.

THE CHAIRMAN: That is the attitude of your company.

MR EVANS: Yes, sir.

MR SHEPARD: I think, Mr. Chairman---

THE CHAIRMAN: Now, Mr. Shepard, in what measure do you disagree with that attitude being taken? -- because, you see, you are going behind that now and talking about what the company received. What do you think should be the proper way of looking at the situation?

MR SHEPARD: I was trying to get Mr. Liddy's opinion, sir, as to whether these assets that were admittedly received should be entitled to earn a rate of return to be earned out of the freight dollar. In other words, the public of Canada donated certain land---

THE CHAIRMAN: Yes. You come down to the measure of compensation for the services which the company renders.

MR SHEPARD: That is right, sir.

THE CHAIRMAN: All right. Well, go on.

MR SHEPARD: I am tying it to this phrase "wages of capital" in paragraph 25, and trying to find out whether the C.P.R. considers that that phrase "wages of capital" would include the capital put into the company by way of arrangement

with the Dominion Government; and I might add that I would think, sir, that there would be a substantial difference between Mr. Evans' illustration of a taxi company or a man giving his son ten taxicabs and land grants by the public of Canada.

THE CHAIRMAN: Well, I think this paragraph 25 is just intended to lay down a certain basic proposition, that capital is in the same class as labour, and you must get something for its hire.

MR SHEPARD: That is right.

THE CHAIRMAN: Then you are trying to find out now, what does the Canadian Pacific deem its capital to consist of?

MR SHEPARD: That is correct, sir, yes.

THE CHAIRMAN: All right.

MR SHEPARD: Q. Would you care to express any further view on that, Mr. Liddy?

A. Well, in answer to the question of the Chairman, our capital for railway purposes is the value of the property that we devote to transportation service right now.

Q. Irrespective of whether that was purchased with the money derived from the sale of securities or whether it was received in the ways that we have already been discussing?

A. That is right.

Q. Then, Mr. Liddy, I would like you to turn to page 109 of Part I. You start toward the bottom of the page there with paragraph 56, which is a general statement from your outline submissions, to the effect that there is a substantial degree of uniformity in accounting methods and statistical procedure between the two major railways of Canada, and then the next two or three pages are devoted to an explanation of the differences that exist

between the Canadian National and Canadian Pacific accounting methods and procedures. I think in the main that you would agree with me, that they consist of differences in the way of handling express, communications and depreciation, and then of course there is in addition the matter of income tax. Would that be a fair summary of the differences?

A. These are accounting differences you speak of?

Q. Yes.

A. There are physical and traffic differences.

Q. Oh, yes, but I am referring now purely to the accounting differences.

A. I think those are the main ones, yes.

Q. Now, would you agree that all those four, all but income tax, are simply a matter of accounting practice? In other words, your treatment of your express operation, your communications and depreciation are all in fact a matter of accounting practice?

A. Depreciation is an accounting practice. The Canadian Pacific of course has a subsidiary called its express company.

Q. Yes, we understand that.

A. It has a separate charter. The Canadian National have not got for their express business a separate company, and when you have separate companies you must have---

THE CHAIRMAN: Q. I beg your pardon?

A. When you have separate companies you must reflect the accounting that is involved in those separate charters.

MR SHEPARD: Q. But there is no reason why there could not be similarity of accounting with or without the charters; the charter is just a legal fiction, after all; it can be disposed of if necessary?

A. It probably could be disposed of. I do not know

what the complications are. We do not feel that it would be a good thing to dispose of the Canadian Pacific Express Company. There was evidence, you remember, in the rates cases, where Mr. Ham said that he felt that separate employees ought to be doing that kind of work rather than railway employees.

Q. You would agree, I take it, Mr. Liddy, that it is really a management decision taken with the advice of their accountants, as to how those three matters will be handled by either one of the two railways -- that is, express, communications and depreciation? It is a management proposition at the moment?

A. Well, the management have made the decision for certain reasons.

Q. Oh, yes.

A. They are not arbitrary.

Q. No, I am not suggesting any wrong motive on the part of management. I just wanted you to agree with me that it was in fact a management decision?

A. I think I can go along with a Yes answer on that.

Q. I wonder whether you would go along with me on this statement, that the object of uniform accounting is to obtain comparability on the operating results, irrespective of the capital structure or the profit and loss statement; I am now speaking of uniformity of accounting between two or more railways, for example between the Canadian National and Canadian Pacific, and I suggest to you that the object of uniformity is to attain comparability so far as uniformity of accounting can do that, between the two railways on an operating basis rather than on a capital basis?

A. Well, I will say this, that you start with operating statistics and operating accounts; that is your start. How far up you ycarry that, I have not really thought it out,

Mr. Shepard.

Q. As far as the classification of accounting is concerned in the I.C.C., one of its main functions, I presume you would agree with me, would be to obtain comparability between the carriers in the United States on an operating basis from year to year?

A. Well, the I.C.C. go further than that, you know.

Q. Isn't that one of the---

A. They have income account and balance sheet, and they go up to seven hundred accounts.

Q. Yes, but you would not disagree with what my question was?

A. You put it on the basis that the main---

Q. The main, yes?

A. Well, I think I would agree with that. You start with that.

Q. The important thing really is to find out how the carriers come out from an operating standpoint at the end of each year?

A. Well, that is getting back to what motives were back of the Interstate Commerce Commission; but it is absolutely essential for the Interstate Commerce Commission, dealing with the large number of railways that they have, to have uniformity or near uniformity; otherwise they could never consolidate the results of the U. S. railways.

Q. Quite. Then, Mr. Liddy, would you turn to page 112 of Part I. Down at the bottom of that page you are discussing communication services, and the third sentence in the paragraph, starting near the bottom of the page, reads:

"Railway service messages - telegraph and long-distance telephone - handled over the facilities of the Communications Department are charged at cost to the

railway and distributed to appropriate operating expense accounts."

I wonder if you could perhaps elaborate a little on the phrase "at cost"; how is that computed?

A. Yes, I would be glad to. I did give evidence in the rates cases as to how that was computed.

Q. Yes; I do not think the Commission has heard it.

A. The cost to the railway of wire service is divided into two parts. One is the maintenance of wires. The railway has certain exclusive use of wires, such as despatchers' wires, and other wires are set apart for the exclusive use of the railway. The railway also requires the use of certain multiple channels.

THE CHAIRMAN: Q. Certain multiple what?

A. Channels, somewhat like a radio. You can send many messages simultaneously over one wire. The cost of maintenance of all wires and property is apportioned between the railway and commercial services.

MR SHEPARD: Q. Is that apportioned on an arbitrary basis?

A. No; on the basis of actual wire mileage or use of channels. The second part is that of the operating cost, in which the communications department bill the railway at the same cost per message for operation as they find it costs commercial services. That is, all messages are counted, railway and commercial, and that is divided into the operating cost. That is a very simple formula.

Q. I gather from your explanation that you are satisfied that your costing with respect to communications is accurately done?

A. Yes. If it is not accurately done it can be improved upon, but we have had this pro-ration of costs for many years, and we have officers in the communications

department who are zealous of their own performance, and they have got together with the railway officers, who have to bear this charge, and they have agreed upon this formula. Moreover, our communications department are required to report to the Board of Transport Commissioners the results of commercial operations, and it is on that basis that they have got to stand up and fight for a rate increase, and if there is any inequality in the formula it can be ironed out. We feel it is equitable. There is not a great deal of money involved in any event in relation to gross railway expenses.

(Page 16898 follows)

Q. Now, Mr. Liddy, at the top of page 113 you refer to the fact that the Canadian National includes in railway operating revenue accounts the gross earnings from commercial communication services, and the C.P.R. do not do that. I wanted to ask you whether you would be willing to do that for the sake of uniformity between the two railways?

A. Would you ask the Canadian National to come to our basis first?

Q. Well, they do not come on until next week; I can ask them then.

A. Well, Mr. Shepard, we have to get around a round table. I don't know where we are going to meet, but the reasons why we have done what we have are very compelling reasons. First of all, you have been through all these rate cases --

Q. One.

A. Well, that is enough. You know then that it is absolutely essential for the railway to have railway costs, and I have not a bit of doubt if we stuck something else in there for commercial costs of sending commercial telegrams that the first thing we would have to do would be to take that out. If we did not the Board would, so why worry about this thing? Why not let us adopt a straightforward plan and get railway revenues and railway expenses exactly like they do in the United States. They have had that system down there for fifty or sixty years. They have had to come to it. There is no need to fool around in Canada with some other different basis. Let us come to a straightforward basis and have railway revenues and railway expenses, and then we know where we stand.

Q. I take it that as to your previous suggestion

[illegible]

[illegible] Wh [illegible]

[illegible] united states [illegible]

[illegible] fitted or sizes [illegible]

[illegible] to it. There is no need to [illegible]

[illegible] with some [illegible] different [illegible]

[illegible] straight [illegible] very [illegible]

[illegible] where we [illegible]

that you would sit around a conference table with the C.N.R. you have not exactly got an open mind on the subject. You have compelling reasons for the way you are doing it now?

A. I have compelling reasons but I think my mind is still open.

Q. There would be some hope from a conference, would there?

A. After all that is the way this world ticks.

Q. On page 114, Mr. Liddy, the last double spaced paragraph, having reviewed the differences between the two accounting systems of the two railways, it says:

> "Such fundamental differences cannot be overcome by uniformity in accounting."

I wanted to get your reasons for that statement. The points that we have been discussing deal with communications, depreciation and express. Leaving out income tax for the moment, you have made the statement that such fundamental differences -- and I presume these are three of what you term fundamental differences?

A. No, I do not think so.

Q. Are they not?

A. Oh, no.

Q. Well, what are they?

A. Read what comes just previously.

Q. Perhaps it would save time if you told me what came previously.

A. Well, it is set out there on page 114. First of all it speaks of the equity interest of the Canadian Pacific and the Canadian National.

Q. You are referring to the difference in the position between a private enterprise and a publicly owned railway?

A. And physical differences.

Q. You are not referring back in that statement to what we have been discussing?

A. Oh, no.

Q. I am just going back to the middle of page 113.

A. It is what immediately precedes.

Q. It is hard to tell what is immediately preceding.

MR. EVANS: Paragraph 57 of the outline submission points out these differences in physical development, and then there is a further submission on that subject.

MR. SHEPARD: Q. Then you go into the subject of depreciation in paragraph 58 commencing at the bottom of page 114, and I want to read a part of that paragraph at the top of page 115 as it gives a summary that will form the basis of discussion with you. It reads:

> "Accruals for depreciable road properties and railway rolling stock are made on the 'user basis'. The annual depreciation charges are developed as a product of the user rates and the use factor. In the case of rolling stock the use factor is the run-out mileage of the various classes of equipment and in the case of road property is the gross ton mileage. Both of these use factors are appropriate measures of the use made of rolling stock and road property, respectively."

The first question I wanted to ask you on the subject of depreciation was whether you knew of any railroad any place in the world that has adopted the user basis?

A. The C.P.R. is the pioneer of all railways.

Q. Other than the C.P.R.?

A. No. I say the C.P.R. is the pioneer in the use of the user basis.

THE CHAIRMAN: Q. Pardon me; that does not altogether answer your question. Has the pioneer been followed by any others?

A. In the United States the railways are required by the Interstate Commerce Commission to follow the same pattern. They would not be allowed to use user unless their regulations are changed. They have given some indication that they are interested in the user basis. The user method is a new method, Mr. Chairman. As a matter of fact, the concept of depreciation is not so old itself. I suppose there has been more development and more understanding of depreciation in the last ten years than what existed in all previous time.

COMMISSIONER INNIS: Q. Do you have a great deal of difficulty comparing your American lines with your Canadian lines?

A. In respect to --

Q. One using the straight line system and the other the user system?

A. For depreciation -- no, sir.

Q. I mean just general comparability?

A. No, we have all these primary accounts. You can compare the cost of ties, the cost of rails, the cost of --

Q. It really does not make it more difficult for you to compare the results of lines in the United States with lines in Canada, the fact that you use the straight line in one and the user in the other?

A. Well, when you take the total result we have got to recognize that one is on the user basis and one is on the straight line, but when you say comparability of results we always go down to the details. We have engineers, for example, interested in the rail program.

[illegible] with [illegible]

[illegible] the standing [illegible]

[illegible] just [illegible] complete [illegible]

[illegible] but [illegible] line [illegible]

They go to the primary account in which they are interested. We have mechanical men. They go to the primary account in which they are interested, and our operating men operating yards or terminals -- they are interested in a particular field.

Q. The problem of regulation of course does not arise?

A. No. In the United States the railways of course have not been strictly on the straight line basis. Perhaps you might be interested in some figures, Dr. Innis, which show just what the United States railways did put into their accounts. I should like to put this in the record in the form of a table. It might be informative. The table is as follows:

U.S. CLASS I ROADS

CHARGES TO OPERATING EXPENSES FOR AMORTIZATION OF DEFENCE PROJECTS AS COMPARED WITH NORMAL STRAIGHT-LINE DEPRECIATION CHARGES

EQUIPMENT - YEARS 1940-1947

Year	Straight-Line Depreciation Charges	Amortization of Defence Projects
1940	$ 196,143,659	$ -
1941	203,270,657	12,714,674
1942	200,712,711	87,483,253
1943	201,473,032	134,259,837
1944	205,469,697	171,097,435
1945	205,947,139	709,381,054
1946	211,336,346	10,162,025
1947	220,556,825	14,802,241
TOTAL	$1,644,910,066	$1,139,900,519

Percent amortization of Defence Projects of normal Straight-Line Depreciation Charges Years 1940-1947 ($1,139,900,519 ÷ $1,644,910,066) 69.3%

Source: Table 158 of Statistics of Railways in the United States.

I simply point to the fact that under the rules of the Interstate Commerce Commission, while they allowed for straight line rates, in another way they allowed for very substantial additional charges.

Q. Was that as a result of income tax regulations?

A. It was the failure of the straight line basis to do a job on the railways.

Q. It seems rather curious it should have come in just during the war period?

A. That is when the traffic was very high, it is true, but it is a recognition of the failure, the inflexibility of the straight line user basis when you come down to a business proposition.

MR. SHEPARD: Q. I suppose it might have something to do with the fact that it was impossible to overcome certain physical depreciation by proper maintenance during the war?

A. I do not see where that is involved at all.

THE CHAIRMAN: Q. What is your answer?

A. I do not see where that question is involved in this matter at all.

MR. SHEPARD: Q. But the I.C.C. still does prescribe the straight line method?

A. Yes. You understand, Mr. Shepard, that having amoritized this expenditure, and it is over the dam as it were, that in future years depreciation now will be less on the straight line basis than what it otherwise would have been. They have taken what you might call a hump in the past few years, and that property is no longer in their depreciable property, and the result is in future years they will have less than true straight line depreciation. They have in effect got exactly the same as we have got on the user basis.

Q. But they are back on the straight line now?

A. Not in effect --

Q. In fact?

A. According to rule, yes.

Q. Then, Mr. Liddy, I should like to refer again to the paragraph at the top of page 115 where you say:

"In the case of rolling stock the use factor is the run-out mileage . . ."

My understanding is there are three types of rolling stock, locomotives, freight cars and passenger cars. Can you tell us what records you have available showing the run-out mileage of these three classes of rolling stock?

THE CHAIRMAN: What are they?

MR. SHEPARD: Locomotives, freight cars and passenger cars.

THE WITNESS: What kind of records would you like me to describe?

MR. SHEPARD: Q. I do not want the size of the page. I wanted to know whether you did in fact have records showing the gross ton miles of locomotives, freight cars and passenger cars?

A. Oh, yes.

Q. You have?

A. Yes.

Q. Are they available?

A. Oh, yes.

Q. And they are actual measured miles, are they?

A. A gross ton mile is the weight of the equipment and contents multiplied by the distance. Is that what you mean by "measured"?

Q. Yes. Do you know the distance that all your cars run?

A. Oh, yes.

Q. All classes of equipment?

A. Yes.

Q. Do you know how far they run in any given year?

A. Oh, yes.

Q. All classes of equipment?

A. All classes.

MR. EVANS: You do not mean gross ton miles; you mean run-out miles?

MR. SHEPARD: Yes, I meant run-out miles. I realize I used the term "gross ton miles."

THE CHAIRMAN: "Run-out miles" is the term used in this paragraph.

MR. SHEPARD: It is run-out mileage in that paragraph, and that refers to rolling stock, and you have such records, have you, of run-out mileage for each class of rolling stock?

THE WITNESS: Yes, we have the actual mileage. Now, there is perhaps one little variation I should mention, that in the case of freight cars that move off our lines -- there is a small percentage that move off our lines in interchange -- we have a record of the car days that those particular cars are off our lines.

MR. SHEPARD: Q. But you do not know how far they run when they are off your lines?

A. We know the number of days they were off our lines, and that is a small arbitrary we add in. We also know the mileage of foreign cars on our line, and that is not taken into consideration.

Q. Because you are not depreciating them?

A. Not depreciating those cars, that is right.

COMMISSIONER INNIS: Q. That would not affect your depreciation on rails or on other accounts?

A. Foreign cars on our lines -- if we were

depreciating rails it would have to be a factor.

Q. It would then be counted in?

A. Yes.

MR. FRAWLEY: If I might presume to interrupt the cross-examination for a moment, Dr. Innis, I should like to read to you a special accounting classification, No. 331½, in Exhibit 182, which was added on September 22, 1941, effective January 1, 1942. It is at page 118 and it is called "Equipment -- Amortization of Defence Projects." It reads:

> "This account shall include the amount of amortization charges accrued during the accounting period for equipment with respect to which the carrier has elected to observe amortization accounting for income tax purposes under Section 124, 'Amortization deductions', of the Internal Revenue Code. The charges so included shall be in conformity with the allowances acceptable to the Bureau of Internal Revenue under the regulations prescribed by it."

I thought I would simply read that in view of your question to the witness as to whether or not it was for income tax purposes.

THE WITNESS: Certainly, Mr. Frawley, they are taken as legitimate expenses in the computation of taxable income, the same as depreciation is.

MR. SHEPARD: Q. Mr. Liddy, you can perhaps correct my recollection if it is not accurate. My recollection is that your evidence in the 20 per cent case was to the effect that the only type of rolling stock on which you had records of run-out mileage was locomotives?

A. No, that was not the evidence. The evidence

was that in respect to individual units locomotives were the only class of equipment for which we had records.

Q. Well, how do you get the mileage for the group without having the mileage of the individual units?

A. Well, that is easier.

Q. Would you explain that?

A. You mean the mileage of passenger cars?

Q. Yes.

A. Well, that is simply a cumulative figure.

Q. Where does it come from?

A. It comes from daily records of conductors of every train operated. That is how we compile our statistics.

Q. It is the total mileage of all cars?

A. All passenger cars.

Q. And then you divide that into the total number of cars; is that correct? You divide the total number of cars into that figure to get the run-out mileage per car?

A. Each conductor reports his train consist. Let us take a simple example of a train running from Ottawa to Montreal. He reports his train consist, the number of each car he handled and the distance he runs, and multiplication gives you the car miles, so many cars, so many miles.

Q. You do that right over the system?

A. Right over the entire system.

Q. On passenger cars?

A. Yes, sir.

Q. So that you get a grand total for the system of passenger car miles run in a given year?

A. That is right.

Q. And to obtain the mileage in a given year per car I suppose you just divide the number of cars in

operation into that total mileage?

A. If you want an average, yes, that is what you do. You take your equipment inventory which would be maybe 3,000 cars and divide that into your total passenger car miles and you get the average mileage per annum per car.

Q. As an average figure only without any reference to the actual physical miles run by any particular car?

A. It is the actual physical miles that make up the aggregate.

Q. But only as an average of the aggregate is your result obtained?

A. That is all we depreciate. We only depreciate the entire group of passenger cars as one group.

Q. Then I should like to deal with the next phrase in that same sentence which reads:

> " . . . and in the case of road property is the gross ton mileage."

Mr. Brazier discussed this with you briefly yesterday. I wondered whether you could tell us how you compute the gross ton miles as a unit of use for your bridges, tunnels, stations and things of that kind?

A. Your question, reduced to its simplest terms, is how do we get the figure of gross ton miles?

Q. Yes.

A. We take every conductor's wheel report, freight, passenger, mixed. We have the weight of every car. We have the contents of every car. We have the distance moved by every car. Those are the prime factors which produce the aggregate of tons by miles.

Q. How do you relate that as a unit of use for something like a station, for example?

A. I do not relate it.

THE CHAIRMAN: Q. What is that?

A. I do not relate it. You are getting back to the same question as the fence.

MR. SHEPARD: Q. Yes.

A. My answer is not "yes" in the transcript in that respect.

Q. Just so that my thinking will be clear on this, on depreciable road property, which includes these matters or items such as we have been discussing, you say that the gross ton mile figure has nothing to do with the computing of the depreciation charge in a given year?

A. No; you asked me to relate it to a particular asset.

Q. Taking a group of assets?

A. Oh, yes, take a group of assets. Take our entire road property.

THE CHAIRMAN: I think it is time to adjourn, but the question before us right now appears to be this. Having regard to the top paragraph on page 115 and the top paragraph on page 116, those two paragraphs taken together, the question is how is gross ton mileage applied, for instance, to a bridge, a station, a fence, and so on? We will discuss it this afternoon.

-- The Commission adjourned at 1.00 p.m. to meet again at 2.45 p.m.

Thursday, March 2, 1950.

AFTERNOON SESSION

S. J. W. Liddy, recalled:

CROSS EXAMINATION BY MR. SHEPARD - RESUMED

Q. Mr. Chairman, when we adjourned, I think we were discussing the question of how the Canadian Pacific Railway determines the gross ton miles as a unit of use on depreciable road property, and perhaps Mr. Liddy can explain the answer that he gave Mr. Brazier yesterday, or perhaps just repeat it, whatever he prefers to do.

A. We covered that question a little bit, Mr. Shepard, at page 115 of Part I of our Submission.

Q. Starting at the last paragraph, is it?

A. Yes. First of all, it covers the rolling stock situation, and the paragraph after that speaks of dividing the estimated number of units of use into the service value of each of the various classes. A user rate was developed for each class, and then it goes on to cover depreciable road property and the Brief says:-

> "In the case of depreciable road property, the user rates were developed in conformity with the same principles as govern the rolling stock calculations, although, in this instance, no estimate was made of salvage value because of the negligible effect on the rate calculation."

And then it goes on at the top of page 116 in the Brief to speak of the broad classes of depreciable road property and that the unit of measure adopted for the allocation between years was the gross ton mile, and then it goes on to speak of inland steamships and work equipment.

Q. Well, my question, Mr. Liddy, was how did you arrive at the unit adopted for the depreciable road gross ton mile unit. How did you arrive at that unit so that it would be a proper unit to apply to something that is really not affected by traffic to any extent?

A. I do not think your question should be why was it as - -

Q. Well, how?

A. Yes. First of all, it is a homogeneous unit covering all traffic. The gross ton mile is a use factor which takes into account freight contents and the tare and it takes in passenger. It takes in all the traffic - mail, express, anything you want, all the traffic on the railway, and it is a homogeneous unit. It is a gross ton mile; it does not vary; it is two thousand pounds multiplied by miles which are exact units.

Q. But isn't what you really think today on the depreciable road property this: you have to, first, make an estimate in years as to the service life of that property, and then you take the additional step and you say: "In some years we have heavier traffic, and, therefore, higher revenues, and, in our view (I am paraphrasing the Canadian Pacific Railway view) - in our view it is more proper to have a higher depreciation charge in those years of higher revenue", but that in effect the gross ton mile unit bears no relationship to the physical depreciation that might be incurred in any given year?

A. No, not necessarily. It has some relationship, but not necessarily so. I would like to refer you, Mr. Shepard - -

THE CHAIRMAN: Would you pardon me a moment? It

seems to me the foundation of all this, is that you allocate the original cost of all these properties over their service lives. That was indicated, that you had something positive in the way of service life of a bridge, station or of a fence. Now, you know the original cost. You know that?

A. Yes, sir.

Q. Now, you have to allocate it, or spread it over something, and you say you are allocating it over the service life of these various items of property. What do you mean by the "service life"? Where do you get that? What is it?

A. Well, that can be expressed, sir, either in units of time - -

Q. I can understand it in units of time.

A. Well, it is the same concept in units of use, because to have fifty million gross ton miles, you must have, on the average, a certain length of time. If, for example, you were to say that the life of a paritcular asset was 500 million gross ton miles, and there were 50 million gross ton miles on the average per annum, that would mean a life of ten years. The very fact that you have gross ton miles, you have not only use but you must have time. You cannot attain units of use instantaneously.

MR. SHEPARD: Would not this be correct? Would it not be correct, Mr. Liddy, that the only way you can get your gross ton mile measure is to make your estimate of service life in units of time and then multiply that by an estimate of gross ton mileage per unit of time, and then you get your total depreciation worked out on the basis of gross ton miles; in other words, it is a rationalization starting with a unit of time and ending up with

a unit of use?

A. Well, outside of technical refinements and improvements, I would say that was a fair appraisal. I really did not want to get into this question of how we exactly arrived at our depreciation rate.

THE CHAIRMAN: I did not hear that last.

A. I really did not want, Mr. Chairman, to get into the technical question of how we exactly arrived at our user rate of depreciation, because it is a technical subject.

Q. I know, but we are trying to see what the technical terms are and how you apply them. For instance, take the gross ton mile and the service life of a rate. When you divide the one into the other, is that to say that the greater the gross ton mile the shorter the life or the longer the life? You see, it is the measure. You see, the unit of measure for the allocation of the original cost of this property over its service life - - it would look as if you knew two things, the original cost and the service life to begin with.

A. The service life is based on an estimate.

Q. Then you have an estimate of the life-time of each one of these pieces of property?

A. Yes, and we also have simultaneously life in units of use. You have one just as simultaneously as you have the other.

Q. Life of use?

A. No, units of use.

Q. In units of use?

A. Yes.

Q. Well, that is just what I am trying to arrive at a full understanding of.

A. May I take you, sir, to Exhibit - -

Q. I can understand, of course, your life in units of time; that is not hard.

A. Yes, that is simple.

Q. But when you measure the allocation over something which you call the "service life" and then have to tell me what the service life means, what does it mean? You must have the two known positives before you can start to measure. You have the original cost, and you have the service life. Then you say, the unit of measure between them is the gross ton mile?

A. That is right.

Q. Now, what is the service life?

A. Perhaps I should take you over Exhibit 181, because I think probably there is a little misconception between us. I would like to go down this list, and you might check off those items of primary accounts which are classified as depreciable and non-depreciable. Well, I think probably it would be sufficient - -

Q. I think, if I remember, ties and rails and so on are non-depreciable?

A. That is right, and roadway small tools are non-depreciable, sir, and all equipment, of course, is depreciable. Now, that gives us for the year 1947, as at January 1, 1948, a total depreciable road property of $322 million. That $322 million includes some $14 million of items such as engineering which are spread over as an overhead to the depreciable and to the non-depreciable property. Now, there are engineering records and estimates. We have taken each one of these individual assets and made an estimate of its life.

(page 16919 follows)

Then we went and we drew a growth trend of our gross ton miles. Now, perhaps I could demonstrate what a growth trend is.

THE CHAIRMAN: Q. Perhaps I have been the cause of leading you into too much of an explanation. Perhaps this will help; if it does not, just tell me. You see, there are three factors here in these first three lines of the second paragraph on 116. You have the original cost of the property, you have the service life, and you have the gross ton miles. Now, it seems to me of those three factors the two that you know are the original cost of the property and the gross ton miles. You know what they are, don't you?

A. Yes, we have a past record of gross ton miles.

Q. Does it not really mean, then, that you determine the service life by an equation between the original cost of the property and the gross ton miles ? Isn't that how you travel?

A. I don't think perhaps---

Q. Or am I wrong in that?

A. I think you would be wrong, sir.

Q. Well, I thought I was going to simplify it for you, but I am not. I am sorry.

A. May I just pass up this rough diagram of the growth trend of gross ton miles? The dotted line is the growth trend; the solid line is the actual record of gross ton miles. Now, that is a growth trend, and if in the year 1950 you look at the growth trend you will see and you will be able to measure mathematically the gross ton miles now being produced as reflecting average conditions at the present moment. That has been a slightly upward trend with the growth of the country. For example, suppose we take the average life of all these assets which I have just gone

over as $56\frac{1}{2}$ years, multiply your $56\frac{1}{2}$ years by your growth trend gross ton miles---

Q. Pardon me a moment. When you give the average life as $56\frac{1}{2}$ years, you are introducing there the element of time, are you?

A. That is an engineering estimate largely, yes, sir, weighted according to these assets.

Q. Once you do that, once you tell me that you have arrived at an average of time life of these properties, I understand the rest of it.

A. Well, you understand most of it, sir.

Q. Well, perhaps I am too ambitious.

A. The point I am trying to bring out is that, having got that past history and that past factual data, with these technical tools such as growth trends we then say what the life of our asset as one group is in gross ton miles, varied or modified in accordance with the views of our engineering department as to what changes will take place, because we are not estimating depreciation of assets in the past, we are estimating depreciation of assets as we now have them and as we will have them for the next few years. Now, sir, I might say that that same plan was gone through in connection with locomotive miles.

Q. With what?

A. Locomotive miles. The growth trend there was taken as the locomotive capacity miles. The growth trend for freight cars was taken as freight car capacity miles. There has been no radical change in the capacity of passenger cars, and we used the straight simple factor of passenger car miles. Then, sir, another technical tool we had was the survivor curve. Those people who know anything about insurance tables will know what a survivor curve means. It is an inverted S curve, and it is

drawn by taking and plotting the percentages of assets remaining in life, remaining in use, and you get a curve. You have on the vertical line the per cent of survivors, and you have on the horizontal line years, and the survivor curve enables you to determine a true average of survivor life, because at any one time you never have a complete record of what life your equipment has; you always have some remaining in service, and if you take any mathematical average of the past you have not taken into consideration what life still exists in the unit you are now using, so you have to resort to a survivor curve. Now, if I have explained this enough, Mr. Sheppard -- I know I am getting into technicalities; I know that this is a matter that we will be willing to go into before the Board with their experts and explain it all to any person's satisfaction.

Q. Don't be afraid of technicalities -- although I particularly do not quite grasp them all now; they will all be written down, you see.

A. Some of that is my fault, sir.

THE CHAIRMAN: Remember we must report on all this.

COMMISSIONER ANGUS: Q. Is it as simple as this in principle, Mr. Liddy -- if you take your automobile you may say the last ten years, on the assumption of driving 9,000 miles a year, but in some years you drive more than that and in some years less, so that instead of writing off one-tenth every year for ten years, you write off in each year more or less according to the distance you are driving in that year?

A. That is essentially exactly what the user basis does.

THE CHAIRMAN: Q. I understand that for a locomotive, but how do you apply it to the other property, what you call road property?

A. It is exactly the same principle. It is the prin-

ciple of allocation, Mr. Chairman.

Q. Because you do not drive your fences around, or your bridges, or your railway stations.

A. No, sir.

Q. It is true you use them.

A. You could have---

Q. But you use them the same one year as another, don't you?

A. Well, the actual physical depreciation of property is not known in any one year. Nobody knows the exact amount of physical depreciation. I bought a house when I was---

Q. I do not suppose that matters, whether you have the straight line method or the user method; there is always great uncertainty?

A. In the end the two results come out the same, and all we say is that for a business proposition, if you relate depreciation to your volume of traffic you have got a rational basis.

Q. If you relate the depreciation to the volume of traffic?

A. In any year.

Q. You will establish then the service lifetime of a given property; is that it?

A. Yes.

Q. That is what I was trying to say. Of those three factors you give there on this page of your brief, it seems to me that is the one you are trying to determine. You have the original cost, you have the gross ton miles, but you have not the service life until you have used those two to compute it; isn't that so?

A. Yes. Well, you estimate, you always estimate service life, either under the straight line method or the

user method.

Q. We are leaving the straight line method aside for the moment.

A. But it is an estimate, sir.

Q. It seemed to me, reading over that page of yours, that those are the two factors which you can ascertain -- the original cost and the gross ton miles?

A. That is a matter of record.

Q. And by the aid of those two you determine the third factor, which is the service life; is that right?

A. Well, no, it is not as simple as that, sir.

Q. I was trying to make it simple.

MR SHEPARD: I think perhaps, sir, I might say a word -- that the gross ton miles, according to my understanding of it, referred to in the paragraph on page 116 would be-- the only known factor they would have would be an annual gross ton mileage, and that would not give the life of any asset in terms of gross ton miles. That known gross ton mileage for a year on the system would not give the service life or any element of the service life of any asset; and my point there -- and I think Mr. Liddy agreed with me and then expanded on it -- was that what they must do in order to get the gross ton mile unit of use is to make their estimate of service life of a depreciable road asset, say a station, and by an engineering survey they determine that it will last for say forty years or fifty years, then they translate, by applying these trends that Mr. Liddy has been referring to, that service life in units of time by multiplying it out with the gross ton mileage that is anticipated during its life.

Q. Is that correct, Mr . Liddy?

A. Well, that is essentially correct, but, you see, if you do that, just that simple way that you mention, you

do not take into effect the fact that gross ton miles is increasing. You have got to go to a growth trend, as I have explained.

Q. That is the trend I have referred to.

A. Yes.

Q. So the gross ton miles I do not believe is a known quantity when it is used with reference to---

THE CHAIRMAN: Except yearly.

MR SHEPARD: Yes, sir; and it does not reflect service life in units of use until you have related it to the service life in units of time.

THE CHAIRMAN: I see. Then you have to introduce the element of time.

MR SHEPARD: Yes, sir.

THE CHAIRMAN: Although this is a user method.

MR SHEPARD: That is right, yes, sir.

Q. Then, Mr. Liddy, I wanted---

A. I was just going to explain how we arrive at the rate then, sir.

Q. Yes?

A. The Board of Transport Commissioners in their judgment of October 1949 took our user rates for road property and they found them reasonable, and they derived a straight line rate from it, 1.77 per cent. You will find that set out on page 6. They say that that is a life of 56 years, tested on the basis of what gross ton miles were produced over a 14-year period of low and high traffic years. Now, let us take that 56 years and multiply it by your factor---

THE CHAIRMAN: Q. Pardon me. Is that 56 years the service life?

A. In units of time.

Q. It is?

A. Yes, sir; and as far as---

Q. Isn't that getting back to what I suggested,-- that is how you arrive at it?

. As far as we are concerned, we think 56 years is a very fair figure. It is a little longer than what the United States railways are using, but, going then to our gross ton mile growth trend and multiplying the gross ton miles by 56 at the year 1950, at the level of 1950 -- not the actual gross ton miles, but the growth trend quantum -- then you get the life of road property expressed in gross ton miles. It may be 500 million. Divide that into your depreciable road property of 322 million, and you have a user rate, so much per million gross ton miles.

Q. It was a necessary part of your problem to determine the 56½ figure that the Board found reasonable?

A. Yes, that was the part; and then we take that and we say, what variation shall we make in that 56 years in relation to traffic output?

Q. Yes, I see.

A. Let me explain it, sir, perhaps, with a locomotive.

(Page 16927 follows)

Q. With locomotives, yes, it is not so hard.

A. It is not quite so hard. That is the only reason I take it. If you find over a period of half years that locomotives have lasted thirty-five years and have made an annual mileage of 40,000 miles --

Q. Are you talking of the average life of locomotives?

A. Yes. You have a mathematical life of thirty-five years, and they have made an average mileage of 40,000. That then is a life in terms of locomotive miles of a million and a half. Now, sir, if by technical changes --

Q. By what?

A. Technical changes in the railway industry you run locomotives twice as fast per year as you did in the past then I say the life will not be thirty-five years.

Q. It will be seventy?

A. It will be some other factor. That is why we come to units of use as a more suitable factor for depreciation than units of time. I would also like to refer you, sir, to the definition that we give on page 117, a definition which deserves careful reading. It is on page 117 of Part I. It reads as follows:

> "Depreciation accounting is a system of accounting which aims to distribute the cost or other basic value of tangible capital assets, less salvage, (if any) over the estimated useful life of the unit (which may be a group of assets) in a systematic and rational manner. It is a process of allocation, not of valuation. Depreciation for the year is the portion of the total charge under such a system that is allocated to the year. Although the allocation may properly take into account occurrences during the year, it is not intended to be a measurement of the effect of all such occurrences."

That simply means if you are depreciating a station you may take into account the actual depreciation, if you could measure it, of that station, but it is not necessary. The system of depreciation accounting is purely and simply a matter of allocating over a period of years so that you build up a reserve totake care of the cost of that property at the time it will be retired.

Q. Does this definition differentiate between the two methods, the user and the straight line method?

A. What that definition really does, sir, --

Q. Is it intended to differentiate or it is just a general proposition?

A. It is intended to say this --

Q. What?

A. That as far as accountants are concerned they do not know what the actual depreciation is.

MR. COVERT: Q. Per annum?

A. Per annum. They only know it over the entire life or average life of assets. A system of depreciation, as long as it is rational and systematic --

THE CHAIRMAN: Q. You mean to say, do you, whether it is based on time or use?

A. Any one.

Q. That is what I say; this definition is comprehensive. It would apply to both methods?

A. That is right, sir.

COMMISSIONER ANGUS: Q. Our difficulty comes a little with this. If you are depreciating in terms of use something that essentially has a life in terms of time-- for instance, if I depreciate a garage in terms of the mileage on the car that might be the most convenient thing to do. You might say, "We will have a garage that will last thirty years and instead of writing off a thirtieth

each year you vary it in accordance with the use that you put it to in the terms of the car's mileage, and if the car was earning your income that is what you might find it most convenient to do, but is that more or less what happens with the fences and so on, that you are taking something that does not itself wear out much faster because it is used more frequently, but you find it convenient to attribute to it the rate of use of the revenue earning assets?

A. Yes, because that is a homogeneous unit. We just find it convenient, and having done that we then have a depreciation cost that varies with traffic volume, a very rational and sensible concept. Now, whatever the rate is or whatever the rate should be, we are willing to amend it or alter it so that there shall be no difference over the years between the straight line rate and the user rate.

Q. Is your system self-correcting in that way? I can see if you estimate the life of something and it may have a shorter life or a longer one, you can see by trial and error whether your estimate is right. Can you do that in the case of the user method applied to things which do not wear out in proportion to the use?

A. Yes, you can do anything with the user method you can do with the straight line method. You have all the facts. I could give this Commission a long list of exhibits that we filed in the three freight rates cases wherein we tested our rates as to their reasonableness, and we produced the estimated service life in years so

that you might compare it with United States roads or any other system, and I think it is fair for me to say this, that in all these exhibits -- and they were over twenty in number -- I do not think there was any successful criticism levelled at our average life that was indicated

by the rates we had been using. The whole point in the freight rates case revolved around the fact that we were in a period of high traffic volume, and the user system produced a charge for depreciation that was higher during those freight rates cases than the straight line rate would produce.

THE CHAIRMAN: All right, Mr. Shepard.

MR. SHEPARD: Mr. McLean has reminded me, Mr. Chairman, that the complaint of the provinces in the 21 per cent case and the 8 per cent interim case was that there was no proof of the propriety of the rate. I was about to come to that point, but I thought perhaps in view of what Mr. Liddy has just said I should put that on the record first.

Q. Mr. Liddy, I presume you would agree with --

THE CHAIRMAN: Pardon me; would you repeat that?

MR. SHEPARD: The basis of our complaint was that there was no proof of the propriety of the user rates struck by the C.P.R.

THE CHAIRMAN: Has Mr. Liddy not covered that ground now?

MR. SHEPARD: There was a motion made before the Board of Transport Commissioners in the 21 per cent case asking for the production of the working papers out of which the C.P.R. arrived at the user rates struck, and in fact used, and that motion was denied by the Board and the working papers were not produced.

THE CHAIRMAN: The accuracy of the figure was in question?

MR. SHEPARD: Yes.

MR. EVANS: My friend, Mr. Shepard, says there was no proof, but I think it perhaps would be fairer to

say that there was none that he accepted. After all, the matter of the rate is, I would submit, for the Board of Transport Commissioners, and if the rate is not satisfactory to my friends and they need some sort of proof, I would submit that is for the Board. I do want to say that there was a great deal of evidence upon which the Board could test the rates, and the reason the Board gave for refusing to order the production of the original studies was based on an argument we made that it is far better to test them in the light of experience than to test them in the light of some forecast before they went into effect. Our position was what good would it do you to go into the detailed studies that preceded this because the studies might prove to be wrong. Is it not far better to test them in the light of experience and see where that leads you rather than to go into the theory lying behind the rate? That was the reason the Board refused the study.

THE CHAIRMAN: Did the Board deal with that in its written judgment?

MR. EVANS: It was an interlocutory matter during the proceedings. I can get the reference though when the Board's judgment was delivered.

MR. SHEPARD: The fact is now that the Board has accepted the straight line method and that we will be developing in argument -- I do not think it is necessary to go into it now -- our reasons.

THE CHAIRMAN: I understand the Canadian Pacific wish to be left free and to have the Board left free also?

MR. EVANS: Yes, but we want to have it clear that we do not expect the Board merely to accept our rates of depreciation without proof. We are quite prepared to offer proof and to have any test applied to them that is fair, but so far as the method is concerned, we

think that if this Commission is going to suggest the adoption of a uniform classification it should give us that freedom to use that method.

MR. SHEPARD: Q. Mr. Liddy, I think probably you would agree that the propriety of the charge in any one year for depreciation is dependent on the propriety of the rates struck?

A. Yes, no matter what basis of depreciation you are on, straight line or user, yes, sir.

Q. And I think all the expert C.P.R. witnesses called in the rate cases stated that they did not know anything about the propriety of the C.P.R. user rates, that they did not examine themselves personally into the propriety of those rates?

A. I think they all tested the rates and submitted evidence.

MR. EVANS: Mr. Dalgleish analyzed the judgment of the Board in the 21 per cent case, and he expressed the definite opinion after his analysis that the disallowance of a portion of the depreciation charged in 1947 by the Board was in error, and he gave reasons for it. It is quite true he did not go into the service life himself and he did not go into all the accounting procedure behind it, but he did analyze the Board's disallowance, and he expressed the firm opinion, to which I will be glad to refer the Commission, that the disallowance by the Board was erroneous, and Mr. Thompson agreed with that.

MR. SHEPARD: There is no question that both Mr. Thompson and Mr. Dalgleish in the 20 per cent application hearings disagreed with the previous disallowance of depreciation as found in the 21 per cent judgment, but I do not think my friends of the railways would say that they also disagreed first with our view that the propriety

of the charge is dependent upon the propriety of the rate.

MR. EVANS: Oh well, we have always agreed with that.

MR. SHEPARD: That is point No. 1. The second point is that these gentlemen, the experts who were called by the Canadian Pacific Railway, had not themselves examined into the propriety of the C.P.R. rates of user depreciation as fixed by the C.P.R. That is the only point I wanted to bring out.

MR. EVANS: They expressed opinions on the method.

THE CHAIRMAN: You mean to say they accepted figures as a working basis without having gone behind them?

MR. EVANS: No, sir, they were called to give evidence --

THE CHAIRMAN: I am asking Mr. Shepard.

MR. SHEPARD: Perhaps I can answer it as I think Mr. Evans was about to. They were called to give evidence on the theory of the user method, and as a matter of theory I do not think there was much between our experts.

THE CHAIRMAN: They did not go any further than the theory?

MR. SHEPARD: That is correct.

MR. EVANS: Our witnesses all agreed that the user method was better than the straight line method. Now then, Mr. Shepard says they did not examine --

THE CHAIRMAN: Did they deal with it in theory from the basis of their own experience?

MR. EVANS: Yes, they knew how it worked. They saw how it worked, but then, as I say, Mr. Dalgleish and Mr. Thompson went one step further. They analyzed the judgment of the Board on the question of the disallowance of certain amounts of depreciation, and they expressed the firm opinion that disallowance was in error

for the reasons they gave after analysis.

MR. SHEPARD: Q. Turning now to another point, I think probably it is common ground between us that your view on the user method is that it more accurately reflects exhaustion of an asset or group of assets by use than the straight line method?

A. I think it does that for equipment. There would not be very much difference between the two methods as to accuracy in respect to road property.

Q. So that as a matter of choice between the two methods, the user basis is preferable where the physical depreciation of the asset can be directly related to the use of the asset?

A. No, you are thinking of valuation now? You are not thinking of a business proposition? You are throwing that out in this suggestion you are making to me?

Q. The suggestion I am making to you is that user would be understandably better where the use factor in physical depreciation is the predominant one?

A. No, no; our submission, Mr. Shepard, is simply that the straight line is a rigid method and is quite unsuited to business conditions, and what is needed is something that is more flexible. In our view the user method, the way we have applied it, gives us that flexibility, but not necessarily any more accuracy in the final result except I think it is easier to apply for equipment, perhaps a little more accurate, but I do not think the choice as to road property has much merit in one system versus another system.

Q. What in your opinion, Mr. Liddy, would be the effect of maintenance levels on the useful life of assets?

A. Maintenance will have an effect on life, but the only way you can estimate life, either in units of use or

units of time, is to take the situation as you have experienced it, the way railways are maintaining their property today. That is the only way you have as a guide.

THE CHAIRMAN: Q. The only way what?

A. The way railways are maintaining their property today. If our standard of maintenance today means that stations will last fifty years that is the only thing you can go on. You cannot assume that twenty-five years from now you are going to have a standard of maintenance that will allow your stations to last seventy-five years, or to let that slip down so they will only last thirty years. Both methods of arriving at service value must take into consideration past experience.

MR. SHEPARD: Q. Would you agree with me, Mr. Liddy, that the use factor in physical depreciation of railroad property is overcome to a considerable extent by maintenance expenses?

A. No.

Q. You disagree with that?

A. Yes.

Q. Entirely?

A. As I say, life of assets can only be estimated on the basis of past experience. I could not tell you how long a rail or how long a station or any other asset may live fifty years from now or twenty-five years from now. I can only base it on past experience, and as we proceed with depreciation and we find life is expanding or contracting, then it is up to accountants to so adjust their rates to reflect that situation as they see it.

Q. But one of the prime purposes of spending money on maintenance is certainly to keep equipment, for example, running. If you do not repair locomotives they would stop running?

A. Well, we have always done that.

Q. And that in effect does to some extent at least overcome the physical depreciation arising out of use?

A. That is why we get thirty-five years out of a locomotive, because we have maintained it.

Q. Now, Mr. Liddy, turning to another aspect --

COMMISSIONER ANGUS: Q. May I ask one question there? Is one of the effects of the user method, assuming the rates are correct and so on, to diminish the fluctuations in net return by charging more depreciation in years with a high volume of traffic and less depreciation in years with a low volume of traffic?

A. Yes, Dr. Angus, you could put it that way. It brings depreciation charges into line with other charges which go up and down with business volume.

Q. Would that in effect give some shelter to the public against the possibility of an increase in freight rates to compensate for a fall in volume of traffic?

A. Yes, that would give some shelter, and during a depression -- that is the time that we do not want to increase freight rates, and moreover the shippers who are shipping freight during a depression may not be the same shippers who are shipping freight during a period of prosperity. Why should shippers during a period of prosperity have a lower rate of depreciation per car mile or per any unit of traffic, than the fellow who is shipping during a depression? It is illogical.

Q. These considerations are more or less independent of, shall we say, the rate of wear and tear on the physical assets?

A. Yes, that is the only basis. While it may have

some side advantages that is not why we are after user depreciation. We think it is just a sound business proposition.

THE CHAIRMAN: Are you turning now to another subject?

MR. SHEPARD: Still depreciation, but it is with reference to their depreciation reserves.

THE CHAIRMAN: I think this may be the time to ask as to methods. What is the attitude of the Province of Manitoba? What do you want us to do? How far do you want us to make recommendations?

MR. SHEPARD: So far as Manitoba is concerned we will be putting forward soon, I hope in the next few days, a suggested amendment of the Railway Act.

THE CHAIRMAN: I think you told me that the other day.

MR. SHEPARD: Yes, sir, and it will include a recommendation that the Board be required to fix the rate of depreciation and the method to be followed.

THE CHAIRMAN: Your amendment will set out the method?

MR. SHEPARD: No, sir, the statute will not set it out. The Board will be required to do it, but it will be dissimilar to the C.P.R. submission. They feel that the carrier should have the option of choosing his own method. We say the Board should prescribe a uniform method.

THE CHAIRMAN: Either the user method or the other?

MR. SHEPARD: Yes.

THE CHAIRMAN: The Board should be free to choose but then its choice ought to become compulsory?

MR. SHEPARD: Yes.

THE CHAIRMAN: All right; we will see your amendment when it comes along, and of course you will give it to counsel.

MR. SHEPARD: Yes, we will. We will have it done as soon as possible.

Q. Then, Mr. Liddy, in your direct evidence I think the figure of $340 million was mentioned as being the present depreciation reserve on the books of the C.P.R.?

A. As at December 31, 1947.

Q. Now, I wondered whether in your opinion transfers to reserves that have recently been made in the last two or three years, other than current accruals, were sufficient to establish the reserve on a sound basis?

A. Yes, I believe our present depreciation reserve reflects all the past accrued depreciation that exists.

Q. And then I think you told us in your direct examination that 36 per cent of that $340 million reserve was accumulated since the institution of depreciation acconnting by the C.P.R. which would be from 1940 to 1947 for rolling stock, and from 1942 to 1947 in road?

(Page 16942 follows)

A. Inland steamships from 1934.

Q. That is 36% of the $340 million?

A. That is right.

Q. Now, if you continued your present accruals or present annual accruals of depreciation which would flow from maintaining the present volume of traffic, would you not have a 100% depreciation reserve in about 20 or 25 years?

A. Did you mean to slip in there the "present volume of traffic"?

Q. Yes.

A. Well, the present volume of traffic is at a high level.

Q. Well, it is supposed to be going higher, isn't it?

A. I beg your pardon?

Q. I thought it was the Canadian Pacific Railway's evidence that they were anticipating increases in the volume of traffic?

A. Yes, but you are going to have more locomotive miles, more carmiles and more investment if you are going to have that, but the present volume of traffic is at a high level, and admittedly the user rates take into income during those periods more depreciation than the straight line basis. Now, if we have the period of a depression or sub-normal traffic, then our depreciation reserve will actually be less than what would be put in there under a straight line basis. It all depends upon the volume of traffic, and if your user rate is not right, we will adjust it so that you will not build up your reserve nor will you let it slip down.

Q. It all hangs on the propriety of the user rate, does it not?

A. The same with any method of depreciation. If you have a 4% straight line rate, there is no virtue in the 4%; it may be 3%.

Q. Except that the straight line rate is based on an estimate of service life in terms of years only, and the user rate is based on that plus a number of other factors that you have been discussing this afternoon?

A. Yes.

Q. And, as I understand it, the straight line method makes automatically the adjustments necessary for changes in inventory value, but the user rate must be recalculated when inventory values change?

A. If there was no change in the average cost per unit of assets, you would never have to adjust your user rate.

Q. Unless you had a change in the number of units as well?

A. Well, you have your miles.

Q. My friend Mr. McLean has reminded me that Mr. Grant Glassco, a chartered accountant from Toronto, when he gave evidence, emphasized the fact that the user rate must be constantly reviewed because of these factors which we have been discussing?

A. I think any rate should be constantly reviewed.

Q. But Mr. Glassco did give that evidence, you recall?

A. He may have. The Interstate Commerce Commission requires United States Railways to change their rates and they do change them practically every other year.

Q. I think it comes to this, Mr. Liddy, that your statement in favour of user, is that the depreciation charges should in fact be geared to traffic which in turn,

of course, is geared to revenue?

A. Yes, we feel that that is a sensible, business-like proposition.

Q. I suppose you would not suggest that the freight rates should be geared to the shipper's ability to pay by the same token?

A. I really cannot get the significance of your question.

Q. Well, if the average shipper's income should be reduced as a result of a period of depression, you would not suggest that freight rates should come down?

A. Well, you should ask Mr. Jefferson that question. I really have no views on how to set freight rates.

MR. FRAWLEY: No views on reducing freight rates.

MR. SHEPARD: Then, Mr. Liddy, I just wanted to ask you a very few questions on the reference you made which appears on page 116. It is the double spaced short paragraph between the two paragraphs from the outline submission. This is Part I:-

> "Recently the Interstate Commerce Commission and the railroads have commenced studying the matter of applying depreciation accounting to track structure, and the Commission's Bureau of Accounts has proposed, that consideration be given to the 'production' (or 'user') method of accruing such depreciation".

Now, there was great doubt left in my mind as to just how far this matter has gone. My understanding is, that it is at the present time simply a basis of discussion. Is that correct?

A. No, I think it has probably got beyond that stage, Mr. Shepard. It has got to the stage where they have taken

the trouble to make a proposed order, drafted it all out verse by verse so that the carriers may thoroughly understand exactly what is proposed.

Q. Is it proposed to put that order into effect without discussion?

A. No, that is the purpose of making it a proposed order.

Q. Well, I would think that perhaps the most satisfactory way to start a discussion on the subject would be to draft an order, and I just wanted to find out whether this is in fact the first step or not. My understanding is, that it is the first step?

A. Well, I do know that the Interstate Commerce Commission and the Bureau of Internal Revenue are anxious to get all the corporations on a depreciation base. To have some on renewal accounting and some on depreciation is to them unsatisfactory, and I think, that while this proposed order does not say so, I think back of it is the thought that the sooner they all get on depreciation throughout the simpler it will be for everybody concerned.

Q. I understand this suggestion you have just been referring to is related only to part of the assets that are now classified as non-depreciable in railway assets. It does not suggest that all of them be placed on depreciation accounting?

A. You mean ties?

Q. I don't know; I am asking for information.

A. It relates to all ties, all rails, it relates to all other track material and to all track laying and servicing.

Q. Does that include all the presently non-depreciable road?

A. Then, if you take this together with the classes that are now depreciable, you would have all property that does depreciate in depreciable accounts.

Q. It would still leave some railway assets not subject to depreciation accounting?

A. Well, land - you can't depreciate land, as I understand it, or earth like in grading.

Q. Have you any view as to whether there is any advantage in adopting depreciation accounting for track, for example?

A. Well, I think it would be a fair method, a fair thing to do, provided that it was realistic.

Q. Well, would not the end result of adopting depreciation accounting be the same as it now is through renewals? In other words, your annual accruals of depreciation would roughly equal out over a period of time the renewals?

A. Well, it would solve one problem we have had in these rate cases, and that is how much deferred maintenance we have.

Q. I don't think that is quite what I had in mind. The question I asked was, that the result of adopting depreciation accounting for presently non-depreciable road would be, that your depreciation accruals each year and year after year would average out to the same amount of dollars as is now being charged by way of renewal to maintenance expenses?

A. If there were no changes in the price structure over the years, yes, but if there is a change in the price level, there would be a difference between the depreciation method and the renewal method.

Q. Because the depreciation method would be based on cost, and the renewal method is based on price at the time the renewal is made?

A. There would be a lag of 20 or 25 years, whatever is the average life cycle.

Q. Then, Mr. Liddy, on page 118, you make reference there to Docket 15100 of the Interstate Commerce Commission, and you quote from three different pages. Page 414 is the second quotation there, and it starts with the words: "Where use is the controlling factor...". That is the phrase I wanted to discuss, coupled with another one which is in the next small paragraph, and which is:- "...if the carriers can develop a practicable plan". Now, I take it that those two quotations are the two question marks that the Interstate Commerce Commission are in fact pointing towards the user method. Would you agree with that? In other words, if you could determine that use is a controlling factor, and if the carriers could develop a practicable plan, then the Interstate Commerce Commission has no fault to find with the user method?

A. Well, this Docket 15100 was dated July 28, 1931. That is 19 years ago, and I think there has been a lot of water spilled over the dam since then. I do not know whether this represents now the views of any of the members of the Interstate Commerce Commission or not.

Q. I don't know either, but all I was doing/to take those two phrases which seemed to me to be qualifications of any approval of the user method and it would seem to me, that the Interstate Commerce Commission at that time said in effect, first of all, use must be a controlling factor;

secondly, the carriers must develop a practicable plan for determining the user rate, and then the user would have the merit that is suggested.

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(Page 16950 follows)

A. The I.C.C. do not seem to have that view today, if this proposed order is any reflection of their views.

MR SHEPARD: Now, Mr. Chairman, I thought it would be just as well to put on the record at this point the references to Mr. McLean's argument before the Board in the 20% Application on this subject of depreciation generally. I do not want to go into it in any more detail than I have, but it is all on the record, and my friend Mr. Evans gave you references to the C.P.R.'s contentions. Manitoba's argument is found in volume 817, starting at page 4409 and running through to page 4460. There is a summary of the objections to the user basis from the viewpoint of Manitoba's approach to the problem, from pages 4455 to 4457 -- three pages there.

Q. Then, Mr. Liddy, turning to page 124, the first full paragraph on that page ends up by making reference to "the hard fact that the railways are under obligation to continue supplying passenger service." Now, we discussed this matter at some length this morning, but there were just one or two other points that I wanted to discuss arising out of that statement.

THE CHAIRMAN: That is a statement that this passenger service is a hard fact?

MR SHEPARD: The fact that the railways are under an obligation to continue to carry it, sir.

THE CHAIRMAN: That the obligation is a hard fact.

MR SHEPARD: Yes, sir.

Q. Now, I take it that you consider it an obligation under -- I think Mr. Evans referred to section 312 this morning of the Railway Act; the railways as common carriers consider that they are obliged to maintain passenger service?

A. Well, I would not want to express my views on

that; I do not think they would be of any use to the Commission.

Q. Well, I think Mr. Evans has already expressed them, so perhaps I can go on. And I think we have reached agreement that passenger rates cannot be raised now because of competition?

A. That was the evidence in the recent rate cases.

Q. But still the obligation to carry passengers is left with the railways?

A. Well, I am in the hands of counsel to say what that contractual obligation is under the R ilway Act.

Q. Now, I wanted to just develop with you a moment: The C.P.R.'s submission as I understand it with respect to grain rates is this, that it is unsound to have any part of the traffic, freight traffic, with rates fixed other than by the Board of Transport Commissioners?

THE CHAIRMAN: Pardon me. Are you going to go into the question of grain rates? Is that what you said?

MR SHEPPARD: Yes, I did, sir.

THE CHAIRMAN: Well, we will think it over.

---(Recess).

---(Upon resuming):

MR SHEPARD: Mr. Chairman, I did not want to imply that I was going to cross-examine Mr. Liddy at any length on the subject of grain rates.

THE CHAIRMAN: No; I knew there was going to be a change of subject, and I thought it would be a good time to take a rest.

MR SHEPARD: All that I wanted to do, sir, was to point out two things: First of all, that with regard to passenger traffic the C.P.R.'s view, as I understand it, is that they are under an obligation to carry that traffic.

THE CHAIRMAN: Yes; they call it the hard fact.

MR SHEPARD: Yes, sir. Then referring on page 188 to item number 4---

THE CHAIRMAN: Well, they are under obligation to carry passenger traffic, are they not?

MR SHEPARD: Well, Mr. Evans quoted I think it was section 312 this morning.

MR EVANS: Mr. Sinclair did.

MR SHEPARD: Mr. Sinclair did, yes.

MR SINCLAIR: Supply adequate facilities for the moving of traffic.

MR SHEPARD: Then, sir, what I wished to do was to relate that statutory obligation, as the C.P.R. puts it forward, to the C.P.R. viewpoint with reference to the statutory obligation imposed on it by section 325 with reference to grain rates. The fourth recommendation in the---

THE CHAIRMAN: That is another hard fact, is it?

MR SHEPARD: Yes, in the C.P.R.'s submission. The fourth recommendation on page 188 of Part I with reference to grain rates, the summary of recommendations, the C.P.R. says this---

THE CHAIRMAN: You are coming to the grain rates, then.

MR SHEPARD: Yes, sir, just for a quick sortie. The C.P.R. says this:

> "If, as a matter of national policy, the grain growing industry in Western Canada should at any time require to be subsidized, the subsidy should be paid directly to the industry by the Government of Canada out of general tax monies."

That is a section that has already been the subject of discussion with Mr. Jefferson, but it does reflect the attitude of the C.P.R. as not being opposed to a subsidy

to the industry, and of course I am not suggesting by commenting on it now that we agree that the rates are not compensatory or anything of that sort, but I did want to draw that statement to the Commission's attention, and then direct one or two questions to Mr. Liddy.

Q. Now, Mr. Liddy, in view of that attitude with reference to grain rates, and assuming that no traffic should be carried by the C.P.R. at a loss -- which I think you would agree is a correct assumption -- would you suggest that it might be fair, or would you consider it unwise, for the Dominion Government to make up any passenger losses that there may be, not as a subsidy but as payment to the C.P.R. for carrying out an obligation imposed upon them by statute?

A. That is, if there was an actual passenger loss?

Q. Yes; this is all on a hypothetical basis.

A. It must be, because it is not my view that there is a loss.

Q. Yes.

A. Well, really that question is beyond my sphere of knowledge.

Q. Well, that is fine. Then there are just a very few questions in Part II, Mr. Liddy, that I wanted to direct your attention to. On page 36 of Part II -- it may not be necessary, Mr. Chairman, for me to ask any questions on this, but I think for the record it should be made clear that the C.P.R. has apparently in writing part of the statements found on page 36 gone on the assumption that Manitoba's submission is that renewal depreciation should be---

THE CHAIRMAN: We are back to depreciation again?

MR SHEPARD: Yes, sir; that renewal depreciation should be adopted for equipment. There is a sentence

starting on the first line of page 36:

"Some idea of the cost of renewal accounting in regard to equipment may be obtained from the fact as proved by the witness Newman in the 20% Case that the restoration of work capacity in equipment alone over the next five years will require the expenditure of an average of $33,200,000 per annum."

MR EVANS: I can assure my friend that that was not the intention of that, if that will help him.

MR SHEPARD: That will.

MR EVANS: The intention there was merely to point to the fact that renewal accounting is not cheaper than depreciation accounting necessarily. I pointed to that because we had a figure readily available to show what would be the charges if we were on renewal accounting for equipment today.

MR SHEPARD: My only point, Mr. Chairman---

THE CHAIRMAN: You point out that on renewal accounting you would have a figure of about $33 million, and with your total accruals and depreciation it would be much less than that, $28½ million.

MR EVANS: Yes. We say that the reason for that is this: Renewal accounting charges expenses the cost of replacement; depreciation accounting does not; it is related to cost.

THE CHAIRMAN: In view of that explanation, what is left, then, Mr. Shepard?

MR SHEPARD: The only point that I wanted to make clear, sir, was that this whole part of the C.P.R. brief is in answer to Manitoba's submissions, largely with reference to depreciation, and Manitoba has not suggested at any time that renewal accounting was proper for equipment. Our submission is that it should be straight line depreciation

accounting, and I just wanted to clarify that.

MR EVANS: But you do, Mr. Shepard, adhere to the idea of renewal accounting for road property?

MR SHEPARD: Yes. Our submission on that, Mr. Chairman, is that it is preferable to straight line depreciation accounting, because it obviates the necessity of checking maintenance to insure that there are no renewals being charged to maintenance at the same time that depreciation is being taken. That is, from the view-point of the regulatory tribunal, it makes it easier to police the accounts of the railways, and that is the reason that we have expressed a preference for renewal accounting on depreciable road property rather than straight line depreciation accounting.

Q. Now, Mr. Liddy, I have just one final matter to discuss with you, and it is on our friend page 27 of the Appendix to Part I, the digest of development. Page 27 is also Exhibit 190. You were discussing, Mr. Liddy, in your evidence yesterday, and I think I remember Dr. Innis asking you a question with reference to the column headed "Rate of Return on Net Railway Property Investment". I just wanted to get your agreement with me that since the advent of serious competition to the railways from other forms of carrier your rate of return has not been nearly as high as it was prior to the advent of that competition. I think it is fairly obvious from looking at that column, and I would ask you if you would agree with that general statement?

A. I think the big factor, Mr. Shepard, in the decline in the rate of return in the latter part of this statement as compared with the first part, is the advent of competition in the railway industry.

THE CHAIRMAN: Q. In what industry?

A. Competition within the railway industry.

MR SHEPARD: Q. You mean competition between rail carriers?

A. Yes, sir.

Q. You do not consider that the development of the internal combustion engine for trucks and buses and the advances that have been made there is a potent factor, and the development of aircraft?

A. It has had its effect, but it is my view that we overbuilt our railroads -- it is not my view; that was the view of the Royal Commission of 1930-31, and---

THE CHAIRMAN: Q. Yes, but you are speaking now in 1950; is that still your view?

A. That we are now just catching up, sir.

Q. I beg your pardon?

A. The country is now just catching up in traffic volume, in line with the railway facilities that are available. We overbuilt our railways in the 1910-1920 period, and Canada has grown, industry has expanded, and the railway mileage has increased only slightly, so that now I think we are coming into a period when the railways may again have traffic density that would be attuned ---

Q. We do not have too much railway mileage now, then -- or do we?

A. Well, not during the war period, no, sir; I would not say we had any too much mileage during the war period.

Q. What about now?

A. Well, we could handle a little more traffic right today.

Q. I beg your pardon?

A. We could handle more traffic today. You see, in the United States the railways handle a density of traffic at least twice what we do in Canada.

MR SHEPARD: Q. You would agree with me, Mr. Liddy, I presume, that you would be handling more traffic today if competing carriers had not been developed in the period from 1920 up to the present time?

A. Yes. There were not very many competing highway carriers in 1920.

Q. Not in 1920, no; but the period subsequent to 1920?

A. You see---

THE CHAIRMAN: Then there was the depression period.

MR SHEPARD: Yes, sir.

THE CHAIRMAN: Q. I see you have the rate of return 1948 the same as for 1935, haven't you?

A. Yes, sir.

MR SHEPARD: Q. Then, Mr. Liddy, there is a column headed "Revenue Passenger Miles (thousands)"; it is the fifth column from the left, including the year column.

THE CHAIRMAN: What is the column? "Revenue Passenger Miles"?

MR SHEPARD: Yes, sir.

Q. I just wanted to point out that the totals there since 1921, or including 1921 to date, with the exception of the war years, have not exceeded the yearly totals from approximately 1910 up till 1920; that is correct, is it not?

A. I think that is a correct statement.

Q. Would you take it from those figures that there is less passenger traffic in total, or that the railways have in fact lost a substantial amount to competing carriers, either on the land or in the air?

A. Yes, I think in passenger traffic that we have lost it, and probably permanently lost it.

Q. Would your forecast be on passenger traffic, then, that it will be worse before it is better, as far as the railways are concerned?

A. I really have not thought about the future.

Q. I think that is all, thank you, Mr. Liddy.

COMMISSIONER INNIS: Q. Would it be your view that the decline or the effects of competition from the Canadian National were particularly effective on long haul traffic?

A. Yes, it would be effective on long haul traffic, but both railways are into practically every community of any size across the whole continent.

Q. Does the effect seem to be so serious as a result largely of rail competition, or to just what particular elements would you attribute the loss?

A. Well, sir, before the Canadian National were unified as one system we interchanged a substantial volume of traffic say with the Intercolonial. We lost that almost immediately the Canadian National were able to give through service from the Maritimes to Ontario and to the west. Also there is the Canadian Northern; at one time they interchanged a lot of traffic with the Canadian Pacific. The Canadian National now are able to serve that traffic from its origination point to its destination point.

MR EVANS: Were you by any chance talking about passenger traffic, sir?

COMMISSIONER INNIS: No; freight.

(Page 16962 follows)

THE CHAIRMAN: All right, Mr. Frawley.

CROSS EXAMINATION BY MR. FRAWLEY

MR. FRAWLEY: Q. Mr. Liddy, yesterday or the day before you expressed yourself as in agreement that there should be a uniform classification of accounts for Canadian railways?

A. We should strive for that, yes, Mr. Frawley.

Q. Mr. Evans said to you:

> "What, in your opinion, would be the first step towards obtaining uniformity in accounting?
>
> A. I think the first step is to adopt a uniform classification suitable for Canadian railways."

So you are not in any disagreement with the rest of us that there should be uniform accounting?

A. No, sir.

Q. I think you will also agree that can only be done by the regulatory body promulgating some uniform classification?

A. I think that is the machinery.

Q. You probably do not disagree with what the Canadian National say at page 80 of their submission which reads:

> "Canadian National submits that there should be a uniform system of accounts for Canadian railways, and that such system should be prescribed in accounting classifications to be issued by the Board of Transport Commissioners under statutory authority."

THE CHAIRMAN: Who says that?

MR. FRAWLEY: The Canadian National.

THE CHAIRMAN: What page?

MR. FRAWLEY: Page 80. I was reading from the paragraph lettered with a capital A on page 80.

Q. That is as you see the machinery, Mr. Liddy?

There first must be -- because I think we are in agreement at the moment that there is no statutory authority or at least nothing plain and direct -- statutory authority empowering the Board of Transport Commissioners to promulgate a uniform system of classifications of accounts?

A. Well, I probably would not agree with you that there is no authority there now.

THE CHAIRMAN: Q. Would you please speak up?

A. I do not think I would agree with Mr. Frawley that there is no authority there now, but in that matter I am entirely in the hands of the legal counsel.

MR. FRAWLEY: Q. You would go this far with me, that if it is there the Board should set up this classification, and if they need the statutory authority you are quite in agreement that they should have it?

A. No objection at all.

Q. I want to call your attention to another phrase in the Canadian National brief on the same page which rather struck me, and with which you will probably also agree. It reads:

> "It is highly desirable that the accounting presentation of its financial position and the results of its operations should be made according to accepted standards."

I take it that is a statement with which you would agree?

A. Are we talking of the Canadian Pacific or Canadian National?

Q. This is a general statement with respect to what is desirable. You are in accord with that as a general statement?

A. Well, I was not the author of that, I am sure.

Q. The Canadian National is limiting it to itself, but I take it you would agree with it? You do not disagree with it?

A. No, but I do not know that it is complete. I would not write it that way.

THE CHAIRMAN: The Canadian National are talking there exclusively as a state-owned enterprise, are they not?

MR. FRAWLEY: Yes, that is right, and they say it is highly desirable that the accounting presentation of its financial position --

THE CHAIRMAN: Of its ---

MR. FRAWLEY: Of its financial position and the results of its operations should be made according to accepted standards. It is the next sentence I particularly want to call to your attention. It reads:

> "A management subject to accountability should not itself decide the accounting rules by which the results of its management are to be judged."

That is a sound proposition, is it not?

A. Leave it to somebody else?

Q. Yes, to the regulatory body?

A. Well, I would like a little string on things like that because I think any corporation has a responsibility to see that its accounts are properly stated, and you must not follow blindly any rule. I think the Canadian Pacific, for example, should never divest itself of the responsibility to issue sound financial statements.

Q. I think perhaps our minds are not meeting at the moment. You are in accord that there should be a uniform classification of accounts issued by our regulatory body, the Board of Transport Commissioners?

A. Yes.

Q. Now, you would be in accord with the proposition

that your management should obey the accounting rules which that system of accounts would lay down?

A. And we would want to see that they are sound.

Q. I simply put it to you that this statement indicates a good reason for it, that is all. You are in accord with it so perhaps we do not need any further reason. You think it is a good thing?

A. Oh, I think uniform accounting is a good thing.

Q. According to rules prescribed by the regulatory body?

A. Well, I have seen some reports which simply say that these results are in accordance with some rules, and to my mind that is a rather ineffective way of saying that these accounts are right.

Q. Mr. Liddy, either you are in agreement with the proposition that there should be a uniform system of accounts laid down by the regulatory body, or you are not. I thought a moment ago you were. You are not receding from that position?

A. Not at all.

THE CHAIRMAN: In so far as that sentence is concerned, I am just wondering whether you are not taking it out of its context. It says:

"A management subject to accountability" ---

Does that mean subject to public accountability? I suppose that is it, Mr. O'Donnell? You are dealing with your own railway and then you go on and say, "a management subject to accountability" --

MR. FRAWLEY: Frankly I thought that first sentence at the top of page 81 was as applicable to the Canadian Pacific as to the Canadian National.

THE CHAIRMAN: Would it be applicable to all corporations?

MR. FRAWLEY: All regulated corporations.

THE CHAIRMAN: I suppose the words "subject to accountability" mean regulated?

MR. FRAWLEY: Yes, that is how I take it.

MR. O'DONNELL: I think if you go further down page 81 to the paragraph lettered B the matter becomes clear.

THE CHAIRMAN: All right; then this brings it back to the railways.

MR. FRAWLEY: Q. Let us go on to page 85.

THE CHAIRMAN: Pardon me a moment. Mr. Frawley, the application that you would make of that paragraph would apply to the Canadian Pacific Railway as well as the Canadian National?

MR. FRAWLEY: That is why I was putting it.

THE CHAIRMAN: Because they are both subject to public accountability.

MR. FRAWLEY: Under the regulatory body, the body that regulates.

THE CHAIRMAN: They have to earn their rates as fixed by a public body.

MR. FRAWLEY: That is my contention. That is why I felt it was as apt to the Canadian Pacific as to the Canadian National.

Q. On page 85 there is a paragraph reading:

> "A considerable benefit would also accrue to any regulatory body with jurisdiction over railway accounting which might be set up in Canada if it were decided to adopt the accounting practices and procedures developed through these joint efforts."

It is referring to the efforts which have been arrived at through the Interstate Commerce Commission and the American Association of Railroads. Would you agree or

disagree with that statement?

A. I think I would agree with that, Mr. Frawley.

Q. It goes on to read:

"Such benefit would accrue largely from the fact that acceptance of what are considered to be standard railway accounting procedures on this continent would tend to keep to a minimum the size of the organization required for the prescribing of accounts and for their maintenance on a basis conforming with changing conditions and improvements in accounting procedures, since the changes prescribed by the I.C.C. could be readily incorporated in the Canadian classification were the account numbers, texts and terminology to follow the pattern of the I.C.C. classification."

You have no disagreement with that statement?

A. No, that is what I say. Let us not go off on a tangent in Canada with some new method or some new principle of accounting.

Q. That is, you would prefer to stick pretty closely to the way the I.C.C. has worked it out?

A. Follow them as they develop and progress.

Q. Mr. Liddy, I would call your attention briefly, and without any danger of repeating at all what Mr.Shepard cross-examined you about, to this fact, that there are in the main three differences in the operating accounts, in any event, of the Canadian Pacific and the Canadian National. One is with respect to express earnings, the other with respect to communications, and the other with respect to depreciation. Are those roughly the three main differences?

A. Yes, I think that is it.

Q. Just for the record let me state briefly that in

the case of the Canadian Pacific the net earnings of the express company by contract are taken into rail earnings?

A. From transportation.

Q. From transportation are taken into rail earnings, and the net earnings from the financial operations are taken into non-rail income?

A. That is right.

Q. And on the other hand, in the case of the Canadian National all earnings are taken into rail?

A. If there are any net earnings.

Q. If there are any net earnings in the case of the Canadian National?

A. That is right.

Q. I do not know whether or not they have any, but if they have any it all goes to rail. Would you agree with what the Canadian National says about its express traffic when it says on page 97:

"The foregoing" --

That is the description of how they handle the matter.

> "-- is strictly in accordance with the Interstate Commerce Commission Uniform System of Accounts for steam railroads which provides that when a railway company transacts an express business through its regular railway organization the revenues therefrom and the expenses thereof shall be accounted for through the primary revenue and expense accounts provided for that purpose."

Is that about the way you understand I.C.C. regulations?

A. Well, as I explained in my evidence in chief there is no express business handled by any United States railway, and there has not been since the year 1939, so how can this be in accordance with the foregoing?

Q. You are quarrelling then with what the Canadian

National says?

A. I do not quarrel with the Canadian National. It is their brief; it is not mine.

Q. You are perhaps questioning them whether or not what they have said as to how they handle it is strictly in accordance with the I.C.C.?

A. I am just giving you the picture of the factual things --

THE CHAIRMAN: Q. What are the facts? This statement in the C.N.R. submission says:

"The foregoing is strictly in accordance with the Interstate Commerce Commission Uniform System of Accounts for steam railroads which provides that when a railway company transacts an express business",

certain consequences shall follow. Am I to understand that you say that the United States railroads do not transact express businesses?

A. There is no express business handled on any United States railway, and has not been so handled since the year 1939.

THE CHAIRMAN: Mr. O'Donnell, does that paragraph refer to past practice?

MR. O'DONNELL: We will have to have it explained by Mr. Cooper.

MR. FRAWLEY: Q. Mr. Liddy, what you say is that if they were transacting an express business then what the paragraph says would be so?

THE CHAIRMAN: When they were.

MR. FRAWLEY: Q. When they were or to the extent that they are now.

A. If any small railway in the United States had some express business the Ineerstate Commerce Commission would not require that railway to segregate its expenses,

but the actual situation in the United States for years and years, as far as my knowledge goes, is that express traffic has always been handled apart from the railways.

Q. I quite agree, but after all it seems to me to be a comparatively simple paragraph. It says:

> ". . . when a railway company transacts an express business through its regular railway organization the revenues therefrom and the expenses thereof shall be accounted for through the primary revenue and expense accounts provided for that purpose."

You do not take exception to that statement? It is a statement of fact?

A. The Canadian Pacific Railway does not conduct --

Q. I am only suggesting to you there cannot be any exception taken to that statement. In the United States when a railway company transacts express business through its regular railway organization then the accounting of the revenues therefrom shall be as indicated on this page of the brief.

MR. O'DONNELL: I think that is in strict conformity with the provisions of account 107 of the I.C.C. classification.

MR. FRAWLEY: Q. I did not understand Mr.Liddy was saying what the paragraph says was incorrect at all?

A. You asked me if I agree that is a good thing.

Q. As to whether it is a fact that is what the I.C.C. uniform system of accounts prescribes?

A. As I understand it the Interstate Commerce Commission's present classification does not even provide an account for express expenses for the simple reason that no railway company has had any need to use such an

account.

Q. I am not quarrelling with you at all, but there might still be a provision in the system of accounts. It might be changed tomorrow, and then there would not be any way of dealing with it?

A. At the present time it is out.

Q. There might still be some provision that says if, as and when such and such happens then certain consequences follow. It is as simple as that?

A. It is as simple as that when I say it is not in the expenses. That is the simple part of it.

Q. Now then, in Canada the express departments of the Canadian National Railway and the Canadian Pacific Express Company are carrying on the same kind of business?

A. I would say so.

Q. Almost identically the same kind?

A. Not perhaps in the same way, but they are carrying on the same kind of business.

Q. I submit to you the nature of the business is almost identical?

A. That is right.

Q. Now, sometimes it is necessary to compare the operating results of the express departments?

A. Yes, there are separate reports made to the Dominion Bureau of Statistics.

Q. And the regulatory body sometimes finds it helpful and even necessary to compare operating results?

A. I would think they would look at those results.

Q. I think you have already said to me, but I put it to you again, that there should be some uniformity in connection with the accounts of the railways?

A. There is in the United States a separate classification for express companies which bears no

resemblance to the railway classification. You see the business is entirely different, Mr. Frawley. They have not any rails and ties, and so on. Their primary accounts are entirely different and their classification set-up.

Q. You are talking of the express companies?

A. That is right.

Q. That is perhaps not my point. Let me try to make myself clear. You agree that there should be uniformity of accounting as between the two express departments, if you will let me use the word "department", of the two Canadian railways, should there not?

A. Well, I really cannot see the necessity of that provided they take it out of railway accounts.

Q. If you will just bear with me for a moment, I am interested in the matter of uniformity of accounts. I am not suggesting for a moment, and perhaps this might put your mind at ease -- I am not concerned whether the Canadian Pacific carries on the ideal system by putting earnings from financial operations into other income and Canadian National does not. I am not concerned with which is the better system. I am simply suggesting to you that they should be the same, either yours or the Canadian National's method of transacting that business. I am putting it to you they should be the same, that there should be uniformity of accounting with respect to these two express operations? What do you say about that?

A. I say take them out and do whatever you want with them after that.

Q. How do you mean take them out?

A. Do not have the cost of picking up parcels on city streets as a cost of railway operation.

Q. In other words, that is your system?

A. That is my theory; that is my belief.

Q. And that is the way it is done with the Canadian Pacific?

A. Yes.

Q. And it is not the way it is done by the Canadian National? That is right?

A. They put it into railway --

Q. Just let us get some agreement. I think we are in agreement about that. You do it one way and the Canadian National does it the other way?

A. Exactly.

Q. I put it to you which ever system may be adopted, by this uniform system of accounts which I am suggesting the Board of Transport Commissioners should formulate, whichever way it is done they should both be done the same?

A. I would hope they would do it the same. You see ours is a separate company --

Q. Let us make some progress. You are in accord with my suggestion that they should be the same?

A. Yes. May I just explain a little further one of my answers to you, Mr. Frawley?

Q. Yes.

A. When you come to study railway statistics and accounts and you have all kinds of averages, revenue per mile of line, expense per mile of line, and so much per car mile, so much per train mile, it is very confusing to have the cost of picking up packages in a truck in your expenses. How can you relate it to car miles and locomotive miles which are on the railway?

Q. Mr. Liddy, will you go along with me as to this, that the Board of Transport Commissioners should have the power, through the instrumentality of a uniform system of accounts which they may want to set up, to decide which is the ideal method, whether, for instance, financial

operations should go into rail revenue or non-rail revenue, and whether or not what you have just told me about the cost of picking up packages, how that should be accounted for -- in any event, the Board of Transport Commissioners should have freedom in the promulgation of this uniform system of accounts to deal with these matters?

A. So far as I am personally concerned I would be glad to sit down with any officers of the Board of Transport Commissioners and attempt to arrive at a uniform classification.

THE CHAIRMAN: We are just about to adjourn. These express companies carry on a variety of businesses, do they not, for instance, a banking business?

MR. FRAWLEY: All of that is called financial operations.

THE CHAIRMAN: You mean in the case of the Canadian National all that is thrown into the railway?

MR. FRAWLEY: The money they earn from the sale of money orders and all of the related operations is taken into rail revenue. That is the crucial difference.

THE CHAIRMAN: We will adjourn now.

---The Commission adjourned at 4.45 p.m. to meet again at 10.30 a.m. on Friday, March 3, 1950.